

UNIVERSITÉ DE GENÈVE
INSTITUT UNIVERSITAIRE DE HAUTES ÉTUDES
INTERNATIONALES

EAST-WEST TRADE AND THE GATT SYSTEM

THÈSE

présentée à l'Université de Genève
pour l'obtention du grade de docteur ès sciences politiques
par

Maciej Kostecki

Pologne

THÈSE No. 296

1977

MACMILLAN
BASINGSTOKE, HAMPSHIRE
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La Commission Mixte, composée des doyens des Facultés de droit, des lettres, et des sciences économiques et sociales, et du directeur de l'Institut universitaire de hautes études internationales, sur le préavis de MM. Gerard CURZON et Jean SIOTIS, professeurs à l'Institut, de Mme Harriet MATEJKA, chargée de cours à l'Institut, et de M. Frieder ROESSLER, *Economic Affairs Officer au Trade Policy Department* du GATT (Genève), autorise l'impression de la présente thèse, sans entendre par là exprimer d'opinion sur les propositions qui y sont énoncées.

Genève, le 27 juin 1977

Pour la Commission Mixte
Jacques FREYMOND
Directeur de l'Institut universitaire



Thèse No 296

To Willi and Maja Roduner

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Biographical Note

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Preface

East-West trade cooperation has been widely debated by economists and others in recent years. But the significant role of the General Agreement on Tariffs and Trade (GATT) in the development of such cooperation has somehow been neglected. This volume, sponsored by the Trade Policy Research Centre, aims to fill that gap.

Czechoslovakia is an original signatory to the GATT. Yugoslavia joined the General Agreement in 1966. Poland, Romania and Hungary acceded to the GATT in 1967, 1971 and 1973 respectively. This last development was an important political event, since it marked a new period in the history of East-West economic relations. Yet the participation of the centrally-planned economies in the GATT necessitated the solution of many purely technical issues. It called for the elaboration of a mechanism to accommodate the East European systems, relying on economic centralisation, to the much more liberal commercial order reflected in the principles of the GATT. As far as Poland and Romania were concerned, that mechanism had to provide, first of all, for a reciprocity formula regulating the exchange of concessions between tariff-protected and target-protected economies. For Yugoslavia and Hungary, who claimed to use tariff protection, an agreement had to be reached on the validity of the traditional GATT approach to reciprocity. Non-discrimination, dumping and safeguard arrangements, also, had to be considered and the respective provisions of the GATT adjusted to new circumstances.

Last but not least, there was the difficult issue of East European economic integration. The centrally-planned economies which joined the GATT maintained their membership in the Council for Mutual Economic Aid (CMEA), sometimes referred to as COMECON (Yugoslavia as an associate member). It was therefore necessary to examine the conformity of CMEA rules and objectives against those of the GATT.

Several years of East European membership of the General Agreement permits a certain evaluation of the suitability of the arrangements adopted. East-West trade cooperation within the GATT thus provides valuable experience which must not be over looked in any

discussion of the new international economic order.

This study focuses on Poland, Romania and Hungary—who are state-trading countries—whose experience in the GATT has been particularly interesting. The relationships of Czechoslovakia and Yugoslavia with the other signatory countries have already been written about, but they are of rather limited significance in a general context. When Yugoslavia entered the GATT, it was no longer a state-trading country in the GATT sense. Czechoslovakia, although now a state-trading country, is a special case; it did not renegotiate its terms of participation in the General Agreement after the state-trading system was introduced in the late 1940s. This study therefore deals with these two cases only in so far as they provide precursory experience for other centrally-planned economies.

Analysis of the technicalities of GATT mechanisms relating to East-West trade accounts for the largest part of this book. Chapters 3 and 4 analyze the traditional GATT concept of trading from the perspective of state-trading systems and the essential features of the Polish, Romanian and Hungarian systems of state-trading, in order to show what types of adjustment were necessary on both sides. The essential institutional arrangements that were designed to provide a framework for East-West trade cooperation in the GATT are re-examined in Chapter 5. Chapter 6 evaluates the impact of these arrangements on trade policies and techniques, both in Eastern Europe and in the West. Finally, Chapter 7 considers some prospects and proposals.

It seemed that these technical analyses should be placed in the context of some wider remarks on the evolution of socialist bloc attitudes towards the multilateral trading system, in general, and the GATT, in particular. Astonishingly little has been written on this topic. These problems, together with a more extensive analysis of the economic and political forces which led to the East European presence in the GATT, are dealt with in Chapters 1 and 2.

The research was carried out at the Institut Universitaire de Hautes Etudes Internationales in the University of Geneva. I am grateful to Harriet Matejka—who closely supervised the work on which this study is based—for her advice, help and encouragement. I owe a special debt to Frieder Roessler and Åke Linden, of the GATT Secretariat, who took a close interest in the general progress of the study. Another large debt of thanks must go to my professors, Gerard Curzon, Jacques L'Huillier, Olivier Long and Jean Siotis, for their comments on earlier drafts.

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In sponsoring the volume, the Trade Policy Research Centre's interest in East-West trade has been assisted institutionally by a grant from the Ford Foundation, in New York, which has also facilitated a number of 'new' fields of enquiry being made for the Centre.

None of the above can be held responsible for the facts and opinions set out in the study. That responsibility is mine alone.

M. M. KOSTECKI

Montréal
August, 1977

Abbreviations

c.i.f.	cost, insurance and freight
CMEA	Council for Mutual Economic Aid; also referred to as COMECON
ECE	Economic Commission for Europe
ECOSOC	United Nations Economic and Social Council
EFTA	European Free Trade Association
f.o.b.	free-on-board
GATT	General Agreement on Tariffs and Trade
GMP	gross, material product
IBEC	International Bank for Economic Cooperation
IBRD	International Bank for Reconstruction and Development; also referred to as the World Bank
IMF	International Monetary Fund
ITO	International Trade Organization
MFN	most-favoured-nation clause of the GATT, expressing the principle of non-discrimination
OECD	Organization for Economic Cooperation and Development
OEEC	Organization for European Economic Cooperation
OTC	Organization for Trade Cooperation
QRs	quantitative restrictions on imports
UNCTAD	United Nations Conference on Trade and Development

Multilateral Trading System and Eastern Europe

The East European attitude towards the post-war multilateral trading system has developed in three stages:

- (1) the rejection of the principles of the multilateral trading order and the rejection of its institutions (1947–55);
- (2) the acceptance of the principles of the multilateral trade order and the rejection of its institutions; and
- (3) the acceptance of the principles of the multilateral trade order and the acceptance of its institutions.

The present East European position is still in the process of evolving from the second stage listed above to the third.¹ The issue involves two elements. The first is the East European attitude towards certain principles of international trade, such as freer trade, non-discrimination, multilateralism and reciprocity. The second concerns the East European attitude towards the institutional pillars of the post-war trade systems – the International Trade Organization (ITO), the General Agreement on Tariffs and Trade (GATT), and the International Monetary Fund (IMF) – which provided, or were expected to provide, an organizational framework for supervising and guiding new developments in world trading relationships.

POST-WAR CONTROVERSY

HISTORICAL PRELIMINARIES

In the Anglo-American view, the post-war international economic order was to be constructed in such a way as to remove the economic causes of friction which were believed to have been at the origin of World War II. This was to be achieved by the establishment of a stable world economy

which would provide all nations with non-discriminatory access to markets, supplies and investment opportunities. Whereas groups of American and British experts discussed the problem of a post-war economic order – and later submitted concrete proposals for multilateral negotiations – the Soviet Union gave the matter no serious consideration and presented no project on the issue. Initially, however, Moscow had been interested in the international conferences concerned with these economic matters. The Soviet delegation took an active part in the Bretton Woods Conference (1944) preceding the creation of the IMF and the International Bank for Reconstruction and Development (IBRD).² Moscow later supported the Western proposal to create an organization for international trade cooperation. The Soviets were expected to participate both in the Bretton Woods institutions and in the future arrangements for multilateral trade.

At that time Washington favoured Soviet participation in the multilateral trading system. The American 'Suggested Charter'³ that was to provide a basic document for discussions at the London Conference (1946) included some provisions directly relevant to the Soviet monopoly of foreign trade (in terms of the Charter – a 'complete state monopoly of import trade'). As compared with American insistence on economic liberalism, in respect of Western governments, these provisions were extremely tolerant towards Soviet economic centralism. They took the highly centralized monopoly of foreign trade in the Soviet Union for granted and offered technical arrangements within which the policies of that monopoly would be consonant with the principles of the 'Suggested Charter'.⁴ This accommodating attitude on the part of Washington stirred suspicions in the Kremlin. Moscow refused to accept the Bretton Woods Agreements despite repeated invitations from the West. The Soviets then absented themselves from the London Conference, claiming they lacked the time to study the Western proposals under discussion. Finally, they stayed away from the Havana Conference and the Geneva negotiations which formulated the Havana Charter (the Charter for the International Trade Organisation) and the General Agreement on Tariffs and Trade.

Since the three East European participants in these conferences (Czechoslovakia, Poland and Yugoslavia) were not at that time state-trading countries, the Soviet absence rendered impossible any constructive discussion of the place of state-trading monopolies in the multilateral trading system. No doubt this constituted an important omission for a conference aiming to establish peaceful trade relations among nations.

The text of the Havana Charter, formulated without the Soviet voice, was supposed to be 'sufficiently flexible' to enable the eventual participation of the Soviet Union in the ITO.⁵ Thus, if the Havana Charter made no specific provisions accommodating a 'complete state

monopoly' to a multilateral and essentially liberal trade order, this was due to politics and not to any impossibility of working out technical solutions for trade cooperation between different economic systems.

CONTROVERSY ON PRINCIPLES OF TRADE

What were the political considerations which kept the Soviet Union and, later, other East European countries away from the multilateral trade arrangements?

In the late 1940s the Soviets believed that the real objective of the American plan for a post-war economic order was to establish the United States' economic and political domination over the world. Non-discriminatory and multilateral trade, freer trade, better investment opportunities, as well as the American plan for major economic aid, were all considered by the Russians to be but strategies in some huge design for a *Pax Americana*.⁶ From that perspective any East European participation in the multilateral trading system carried with it a danger that the United States might expand economically and politically into the Soviet sphere of influence.

Another factor that strongly influenced the East European attitude was the expectation of economic crises in the post-war Western world.⁷ For that reason the East European governments preferred to put off deciding on terms of economic cooperation with the West. In their view, the Western countries—threatened by unemployment and over-production—would become much more receptive to demands for favourable loans and supplies. Moreover, the Soviet expectation of an economic crisis in the West led the leaders in the Soviet Union to prefer bilateralism as a more advantageous form of trading.

Paul Baran, the economist, commenting in 1947 on Soviet trade policy, wrote:

Dealing with countries competing with each other for the Russian market, the Soviet foreign traders may be in the position to strike favorable bargains with individual countries, conclude barter and clearing agreements, and secure special advantages in the terms of trade, etc. Many, if not most of these possibilities would be precluded by the ITO charter.⁸

Soviet reluctance to accept the principles of non-discrimination and multilateralism in the late 1940s could also be explained by the desire to develop a system of bilateral economic arrangements within Eastern Europe. Participation in the ITO or the GATT might render this aim more difficult. Multilateralism and non-discrimination could call for an orientation of East European foreign trade quite different from the politically desired pattern. The Kremlin also believed that one of the

Western objects in promoting freer trade was to hold on to markets for industrial products in the less developed countries and check their industrialization.⁹ East European governments considered that protection was necessary for the industrialization of their countries. That industrialization, in turn, was believed to be a condition *sine qua non* to free Eastern Europe from imperialist domination by Western powers.

The Soviets also suspected that the multilateral trade order, as designed by the General Agreement and the Havana Charter, went against the interests of small and intermediate traders. The East European governments thus did not see much advantage in participating in such a system.

Finally, there existed at that time certain contradictions between the Western concept of non-discrimination and multilateralism, on one hand, and the method of country-specific planning in the Soviet foreign trade sector, on the other. Compliance with non-discrimination could require certain reforms in East European planning methods.

The East European criticism of non-discrimination and multilateralism as embodied in the Havana Charter and the GATT was voiced in the United Nations in 1948.¹⁰ The centrally-planned countries maintained that formal application of non-discrimination in a world where some countries were rich and others poor resulted in the economic and political dependence of the weaker partner on the stronger one. In their opinion a different meaning should have been given to the term non-discrimination from that expressed in the General Agreement or in the Havana Charter. Non-discrimination should not restrain any country from determining the form of its economic relations in its own best interest.¹¹ The East Europeans argued that any unilateral action introduced for non-economic reasons (as for example, the United States embargo on exports to Eastern Europe) should be considered a discriminatory trade practice.¹² Moreover, the Soviets, who had practised and preached multilateralism and non-discrimination before the war, now maintained that bilateralism did not conflict with their understanding of non-discrimination. They argued that bilateralism could prove advantageous to poor nations seeking equitable distribution of gains from trade and better access to supply of industrial equipment; bilateralism could turn out to be an effective weapon for countries which, though poor, were important exporters of certain raw materials in great demand on the world market.¹³ Whereas multilateralism and formal non-discrimination could require exports of scarce raw materials to a number of countries, the exporter of a scarce material would have greater bargaining power when dealing bilaterally with only one country.

Oskar Lange, the Polish economist, while speaking at the Third Session of the General Assembly, concluded on similar grounds that the condemnation of bilateralism in the Havana Charter was not fully

justified. Karin Kock, a Swedish observer, rightly noted, however, that Lange interpreted bilateralism not as the balancing of payments between two partners (as it usually is understood), but rather as an exchange of goods in values previously agreed upon between two partners. Moreover, Lange's statement should be placed in its historical context – the scarcity of raw materials and intermediate goods, political discrimination such as the Western strategic embargo on exports to Eastern Europe and East European political discrimination against Western goods – these were the characteristics of international trade in the late 1940s.¹⁴ The East European desire 'to add "discrimination" to the growing list of words whose meaning had been twisted and perverted' was heavily criticized in the West.¹⁵ The project of resolution, supported by the centrally-planned economies, was refused at the United Nations forum.

In that context, what must have appeared most astonishing was the sudden change in the East European attitude towards the principles of multilateral trade which followed several years later. Indeed, by the early 1950s some 'softening' of the Eastern trading area's position may be noted, and in 1955 the same governments announced in the United Nations Economic and Social Council (ECOSOC) their conversion to multilateralism and non-discrimination.¹⁶

This change in the East European attitude grew out of a complex of political and economic developments. The centrally-planned economies now realized that an international trade order promoting freer trade, non-discrimination and multilateralism would be in the interest of small and middle-sized trading nations and that it was, indeed, these countries which derived the most important economic advantages from participation in the system.¹⁷ They hoped that their conversion to non-discrimination and multilateralism would considerably loosen the controls regulating the export of strategic goods to the Eastern trading area and reduce discrimination against East European products on Western markets. Events had also disproved the suppositions of East European economists concerning the inevitability of profound economic crises in the West, at least for the post-war period. The centrally-planned economies no longer wanted to postpone agreements on terms of economic cooperation with the Western industrial nations.

Although the above-mentioned tactical considerations are not to be discounted in the East European conversion to non-discrimination and multilateralism, there were other more important reasons. In the mid-1950s there was considerable modification of the way socialist governments viewed their political self-preservation in Eastern Europe. Broadly speaking, once the bipolar structure of world relations had been established, participation in a multilateral trading system no longer seemed (in the opinion of many East European leaders) a direct threat to Communist power. These new circumstances permitted a return to the

Leninist theory of peaceful coexistence which may be summarized as follows: since socialism prevails first of all only in some, not all, countries, one must imply the necessity for a period of coexistence between countries with a socialist system and those with a capitalist system. This led Lenin to recognize the need for peaceful coexistence between the two systems as the only option left if peace were to be maintained.¹⁸ Consequently, the Stalinist doctrine of two international markets (socialist and capitalist) could not be considered an ideological necessity.

The post-Stalinist period in Eastern Europe has been characterized by greater concern with economic policy objectives such as development of the technology-intensive industries and raising the standard of living. These objectives required, first of all, important modifications in planning techniques. In the foreign trade sector, progressive decentralization and the introduction of more objective criteria for foreign trade efficiency made socialist managers more conscious of discriminatory tariffs and the other obstacles to East European exports to Western markets. Those ministries and managers of foreign trade enterprises, who were expected to apply the new foreign trade criteria, exerted considerable pressure on political authorities to formulate a new East European commercial policy towards the West. Foreign trade had come to be recognised as an important factor of socialist economic development. From the mid-1950s on, the Soviet Union and other East European countries began to follow a long-term policy aimed at extending their trade with the developed market economies. The improved commercial relations between East and West were expected to provide East European enterprises with better access to Western technology and an important source of investment and consumer goods.

The diplomatic action of the East European countries which followed in 1955 in the ECOSOC was a direct result of the above developments. The change of the East European attitude was justified on the international forum by new conditions of world trade relationships. The Soviet Union claimed that, whereas in the early post-war period bilateralism had been the best way of achieving the United Nations aims in the economic field, at the present stage of international trade multilateralism and non-discrimination were necessary for the continued development of world commerce.¹⁹ Guided by this idea, the Soviet Government appealed to the United Nations members to ratify the Havana Charter, which was, in the Soviet opinion, the only realistic way of establishing healthy conditions for international trade.

The Soviet proposal met with mistrust among the Western governments which considered the Havana Charter a dead letter and refused to continue discussion on the issue. It was claimed in Western political circles that the new East European initiative was a tactical manoeuvre to get rid of the Western economic embargo. This interpretation of the East

European conversion to the principles of multilateral trade is certainly too restrictive. As noted above, East European leaders were inspired by motives going beyond tactical considerations. Eastern Europe's conversion to multilateralism and non-discrimination reflected *détente* in East-West relations and a modification of the Eastern bloc's strategy towards economic cooperation with the West.

EAST EUROPEAN CONCEPT OF TRADE ORGANIZATION

Since the Soviet Union and some other East European countries had finally come to accept the principles of multilateral trade underlying the GATT-IMF system, why did they not immediately join the two institutions?

The Soviet Union and the United States did not share the same concept of international trade organization. The United States, having a dominant position in the international economic sphere, desired an international trade organization isolated from any political environment. The American administration and governments of the other industrial countries held that economic cooperation should be discussed and resolved in its own realm, without intruding into other areas of policy. In this way, they defended what Richard Cooper, the Yale economist, called a 'two-track system': economic issues would travel on their own track, not interfering with traffic elsewhere.²⁰ The Soviet Union, on the other hand, as a leading political and military power, but rather a medium-sized trader, preferred an institutional framework where the political and commercial tracks could interfere with each other. This observation is of primary importance for understanding Soviet policy towards the GATT, the IMF and other international economic organizations.

Already in its first criticism of the post-war economic organization pronounced in 1948, the Soviet Union underlined that the IMF and the World Bank were too independent of the United Nations' political bodies to be capable of properly fulfilling the objectives of the United Nations Charter. In an effort to restrain the importance of these organizations as pillars of the post-war economic order, the Soviet Union maintained that ECOSOC could function as a central forum for discussion of international economic problems.²¹ Moreover, the Soviet desire to challenge the competence of the IMF and the GATT seemed to be a motivating force behind Moscow's initiatives in the creation of a new European body for trade cooperation, as well as later proposals for the creation of a comprehensive trade organization.

The growing bipolarity of the international system in the late 1940s and the early 1950s placed the IMF, the IBRD and the GATT decidedly in the West. Poland withdrew from the IMF and the World Bank in 1950. Czechoslovakia was compelled to withdraw from the same two

organizations in 1954. United States leadership was established in the IMF, the World Bank and the GATT; these organizations then carried out policies that the Soviet Union considered as an extension of American political thinking.

In the mid-1950s better conditions for a new dialogue were created by the thaw in East-West relations. It was precisely in 1955 that the Soviet Union appealed in the ECOSOC for ratification of the Havana Charter and creation of the International Trade Organization based on the provisions of this Charter.²² The fact that the Soviet Union did not consider accession to the GATT, but rather preferred to push for creation of the ITO (based on rules essentially similar to those of the GATT), meant that the ITO—as a trader's forum—had to be more advantageous to the Soviets. Indeed, whereas the GATT in the mid-1950s was relatively limited in its membership, consisting mostly of the developed countries critical of Soviet foreign policy, the ITO was expected to be based on universal membership. Moreover, the ITO, as distinguished from the GATT, was conceived as a United Nations organization, and its charter provided for the establishment of an effective link with political organs of the United Nations.²³ Finally, the Havana Charter included some specific provisions on the state-trading systems. The Soviet Union considered that participation in an organization that had adopted a general solution for state-trading countries was preferable to participation in the GATT which would make special arrangements on a country-by-country basis.

Almost simultaneously with the discussions on the ITO in the ECOSOC, efforts were undertaken for the creation of the Organization for Trade Cooperation (OTC) under the auspices of the GATT. This project, however, did not meet either Soviet or American expectations.²⁴

The Soviet-American divergence of views on the matter of providing an institutional framework for international trade reappeared in the report of the group of experts presented in May 1963 to ECOSOC.²⁵ The group of experts, influenced by the East European viewpoint, called for the setting up of a completely new United Nations agency, having universal membership and large powers in the sphere of international trade.²⁶ The organization was to be inspired by the guiding principles adopted at the United Nations level. It would implement in particular the various recommendations of the United Nations Conference on Trade and Development (UNCTAD) as well as other relevant policy decisions taken by organs of the United Nations. The project envisaged a place for the GATT in the organization as its committee on tariffs.

The above proposal did not meet with much interest among the major trading nations. Nevertheless, due to East European intervention, the General Assembly resolution establishing UNCTAD as an organ of the Assembly provided that UNCTAD should also be concerned with

matters relating to the elaboration of a comprehensive trade organization.²⁷ From 1970 onwards, some new initiatives in this regard have been undertaken by the centrally-planned economies.²⁸

It is impossible to assure the proper functioning of a comprehensive trade organization without the active support of the economically strong countries. For the moment, therefore, creation of such an organization remains an item for discussion rather than action due to lack of support among the Western governments. The GATT membership certainly is a second-best solution for the socialist countries seen as a bloc. The impossibility of creating a comprehensive trade organization without the support of the West made some of the Socialist countries accept the GATT for reasons discussed below. Nevertheless, the socialist bloc's strategy in matters of international trade order is still likely to remain one of aiming at the creation of a comprehensive trade organization responsive to political pressure.

EAST-WEST TRADE AND THE GATT

THE GATT AS A WORLD TRADE ORGANIZATION

In the late 1950s, however, since the creation of a comprehensive trade organization had failed and the intensification of East-West commercial relations necessitated a traders' forum and commonly agreed code of conduct, the centrally-planned economies turned to the GATT.

At the time of writing, six centrally-planned economies are already members of the GATT (Cuba, Czechoslovakia, Hungary, Poland, Romania and Yugoslavia), five of which are state-trading countries (all but Yugoslavia). The state-trading countries which are party to the General Agreement, however, account only for about 4.5 per cent of the GATT's trade as compared with the 75 per cent share of the Western market economies. Since the GATT is more a traders' forum than a political organization, a country's importance in international trade determines the extent of its influence in the General Agreement. Accession of the centrally-planned and developing countries to the GATT, even if impressive in number, could not alter the role of the Western industrial countries as they account for a prevailing share of GATT trade. The total number of contracting parties to the General Agreement is 83, as compared to 22 in 1948. A further 15 countries apply the GATT *de facto*.

It may be useful, at this point, to mention some aspects of the General Agreement which are relevant to the study, but will not be taken up later in the discussion of the socialist countries' accession to the GATT.

The general 'house-keeping' of the GATT is handled by the Council of Representatives.²⁹ Administrative functions of the organization are

assumed by the GATT Secretariat, headed by the Director-General (for the first twenty years Sir Eric Wyndham White who was succeeded by Mr Olivier Long). The improvised organizational structure of the General Agreement depends heavily on numerous committees and working groups. They investigate significant problems and submit reports either to the Council or to the sessions of the Contracting Parties (the signatory countries in formal session). Sometimes, the GATT has recourse to the help of experts or panels of experts acting in a personal capacity.

Starting in the late 1950s, the GATT's intensive search for pragmatic response to new trade relationships and political pressures was reflected in a series of reviews and amendments. Due to the growing concern of GATT members with state trading in their own essentially private-enterprise economies, some new provisions on state trading were introduced in 1957. There were also significant changes resulting from the pressure of the developing countries for more equitable commercial relations. These were first – in 1955 – introduction of some amendments to Article XVIII (General Assistance to Economic Development) and later – in 1963 – a new Part IV on trade and development.

In the field of industrial products, the GATT came close to total elimination of quantitative restrictions. Concurrently, there were almost continuous negotiations for tariff reductions. During the Dillon Round (1960 – 62) and especially the Kennedy Round (1964 – 67) remarkable progress was made in the elimination of tariffs in world trade.

It was certainly the GATT's efficiency in dealing with practical commercial problems that first attracted the attention of the East European governments.

EAST EUROPEAN INTEREST IN THE GATT

From the mid-1950s onwards, East-West trade enjoyed a high rate of growth: it increased faster than overall world trade, faster than trade within the CMEA and faster, too, than trade among the industrialized nations. In spite of this impressive growth, however, the relative importance of East-West trade was very low. Indeed, in the 1960s, the CMEA countries' trade amounted only to about 10 per cent of world trade.

East-West trade accounted for an even more modest percentage of world trade. In 1955, trade between the developed countries and the CMEA countries comprised a mere 1.5 per cent of total world trade; and by 1970, that share had increased only to 2 per cent.

In spite of dynamic growth, it was widely felt that the level of East-West trade was too low. Certainly the fact that a given country accounts for a certain percentage of world-wide industrial production does not mean that it should account for a given percentage of world trade. It is

worth noting though, that the CMEA countries accounted in 1970 for about 30 per cent of the industrial production of the world and the developed market economies for about 60 per cent.

The East European countries' interest in international trade arrangements was motivated by their desire to develop trade relations with the Western world. East European policy followed two different tracks. First, a common front of the socialist bloc was maintained on the United Nations forum, especially in the Economic Commission for Europe (ECE), which aimed at reaching some agreements on trade matters with the Western governments. Second, individual East European governments started to seek closer contacts with prevailing Western economic arrangements. In the late 1950s and early 1960s, efforts of *rapprochement* were undertaken individually by the Soviet Union, Poland, Hungary and Czechoslovakia, *vis-à-vis* the Organization for European Economic Cooperation (OEEC), the governments of the European Community and the Organization for Economic Cooperation and Development (OECD) which replaced the OEEC.³⁰ East European interest in the GATT falls into that trend of pragmatic policy aimed at establishing closer individual links with essentially Western economic arrangements. The most significant developments in relations between East European countries and the GATT are presented in Table 1.1

TABLE 1.1
Chronology of Relations between East European
Countries and the GATT

	1948	<i>Czechoslovakia: original member of the GATT</i>
	1950	<i>Yugoslavia: observer in the GATT</i>
October	1957	<i>Poland and Romania: observers in the GATT</i>
	1959	<i>Yugoslavia: associated member^a</i>
November	1959	<i>Poland: associated member^a</i>
	1962	<i>Provisional accession of Yugoslavia to the GATT</i>
March	1965	<i>Poland formally admitted to participate in the Kennedy Round</i>
	1966	<i>Yugoslavia: full member in the GATT</i>
November	1966	<i>Hungary: observer in the GATT</i>
June	1967	<i>Bulgaria: observer in the GATT</i>
October	1967	<i>Poland: full member in the GATT</i>
November	1971	<i>Romania: full member in the GATT</i>
September	1973	<i>Hungary: full member in the GATT</i>

^a By association is meant acceptance to declare relations open between the country in question and the Contracting Parties of the GATT.

It is interesting to relate the chronology of the East European relations with the GATT to trade statistics. Poland, which was the first CMEA country to join the GATT after the Cold War period (Yugo-

slavia not being a full member of the CMEA), had the highest share of Western imports in total imports. From the mid-1960s on, there was an important increase in the share of Western imports and exports in Romania's foreign trade. Romania was the second CMEA country to negotiate its accession to the General Agreement. Finally, Hungary – the third CMEA country which negotiated its accession to the GATT – ranks third in the CMEA in regard to the importance of its trade with the West as a percentage of total trade.

Indeed, the East European motives underlying accession to the General Agreement were mostly of an economic nature. The principal concern of the East European governments in trade with the West was Western discrimination, especially discriminatory customs tariffs, quantitative restrictions (QRs) and strategic embargo. Tariff discrimination was largely due to the fact that the East European countries did not enjoy the most-favoured-nation (MFN) treatment on some Western markets.³¹ In any case, the MFN clauses maintained by the Western states in relation to the centrally-planned economies were less extensive than the MFN clause of the General Agreement. Whereas the MFN clause of the bilateral agreements referred mostly to tariffs, the MFN clause of the General Agreement had a wider scope – covering tariffs as well as quantitative trade control measures and some other matters. The MFN clause enjoyed by some of the centrally-planned economies in the West was also much less stable. Its formal application expired with the validity of a particular bilateral arrangement. It could be withdrawn any time in cases where it had been accorded unilaterally or applied only *de facto*. Finally, tariff concessions accorded on the basis of bilateral arrangements, outside the GATT, could be more easily suspended than those under the GATT.

Moreover, countries that accorded MFN treatment to East European countries on a bilateral basis could refuse to grant them any additional concessions agreed upon subsequently in multilateral trade negotiations under the auspices of the GATT. They could, for example, claim that since a particular East European country did not participate in multilateral negotiations, the principle of reciprocity did not apply in relations with that country. Consequently, whether or not a country benefited from concessions agreed upon during multilateral negotiations could be conditioned by that country's participation in these negotiations.³² Accession of the centrally-planned economies to the GATT would thus considerably broaden these countries' benefits from MFN treatment.

Another important problem that East European governments expected to solve through the GATT was Western discrimination against their exports through the maintenance of quantitative restrictions. The discriminatory QRs on East European exports were often justified in the West on the following grounds. It was claimed that the discriminatory

QRs were necessary to prevent disruption of the Western markets by East European exports. In addition, it was argued that the discriminatory QRs were required to escape the danger of 'dumping' by the East Europeans.³³ Since the East European governments were convinced that the points in question were unfounded, they preferred that the issue be taken up in the GATT and on the basis of the GATT provisions on dumping, market disruption and quantitative restrictions.

Another aspect of the unfavourable impact of the discriminatory QRs on East European exports resulted from the complicated bureaucratic procedures involved in their enforcement. A fear, also, that the discriminatory QRs would be increased in the future, introduced an element of risk in East-West commercial relations. It was, thus, hoped in Eastern Europe that accession to the GATT would create conditions for elimination of discriminatory West-European QRs.

Creation of the European Community also played its part in East European interest in the GATT. The establishment of this Community posed certain threats to the development of trade between East European countries and the European Community's members. Since agricultural products accounted for an important share in Polish, Romanian and Hungarian exports to the Community, the common agricultural policy was of particular concern to the East. The Community's common agricultural policy was discussed in a number of GATT committees and working parties. It was expected that GATT members would obtain important concessions (either in the form of modification of the common agricultural policy or through compensation in terms of market openings for other products) from the Community. Thus, East European participation in the GATT offered an opportunity to compensate, at least partially, for market losses sustained by some centrally-planned economies due to the creation and subsequent enlargements of the European Community.

Moreover, the progressive decentralization of foreign trade systems in Eastern Europe and the introduction of more objective criteria of economic efficiency increased East European concern with the considerable degree of bilateralism in East-West trade. The GATT, which propagated multilateral and non-discriminatory trade, was in accord with these shifts in East European trade policy.

Finally, the forum of the GATT provided a framework for conciliation and the machinery for settling differences on commercial matters otherwise lacking in the East-West sphere. East European membership of the General Agreement certainly also helped to arouse the interest of Western small- and middle-sized businesses in trade with Eastern Europe. Soviet reluctance to join the GATT may be explained, as noted before, on political grounds. The Soviet Union ranked relatively low among the trading countries and the GATT did not

provide an appropriate framework for establishing Soviet influence in the international trading system.³⁴ Even the purely economic considerations motivating the Soviet attitude, however, were different from those influencing other East European countries. First of all, the Soviet Union was much less dependent on trade with the West than the other centrally-planned economies.³⁵ Moreover, as a large economy, the Soviet Union was in a much better bargaining position, *vis-à-vis* its Western counterparts, than the other CMEA economies. Finally, a certain scepticism persisted in the Kremlin as to the GATT's usefulness to state-trading systems. One example of Czechoslovakia's membership of the General Agreement, based on a tariff approach, could not be very stimulating for other target-protected economies. Soviet authorities refused participation in the GATT on the basis of special arrangements such as were adopted for Poland and Romania.³⁶ The Soviet opinion was that participation on these terms would have amounted to accepting second-class membership.

For Poland, Romania and Hungary, membership in the essentially liberal GATT had quite another political meaning. On the one hand, it testified to a new flexibility of alliance within the Eastern bloc, permitting individual East European countries greater independence in their foreign policy. On the other hand, this *rapprochement* coincided with the softening of Soviet criticism towards the General Agreement. The last open criticism of the GATT by a leading Soviet official had been pronounced in 1960.³⁷ Since then, the Soviet Union had adopted a more tolerant attitude towards the GATT. It admitted that participation in the General Agreement could bring commercial advantages to some East European countries.³⁸

ATTITUDE OF THE WEST

No doubt, the *rapprochement* between some East European countries and the GATT was also made possible by changes in the American and West European view of East-West relations, resulting from a better political climate. The West now recognized that intensification of economic contacts with centrally-planned economies could be a positive development, provided that East-West trade policy was subordinated to the objectives of East-West foreign policy. According to this view, trade with the East was to become an instrument for the modification of Eastern Europe's centrally-planned systems and a means of helping some of those countries to increase their relative independence within the Eastern bloc.

Broadly speaking, the new *Ostpolitik* followed three principles. First, the West abandoned its all-or-nothing policy in its relations with the centrally-planned economies. Sudden transformation of these economies into liberal societies was judged impossible. Gradualism was

adopted as more realistic. Secondly, the West stopped thinking about Eastern Europe en bloc. Differences among the East European countries were recognized to exist and Western policies were adjusted to each particular case, even if this meant treating some countries less favourably than others.³⁹ Thirdly, it became conceivable that the West might stop judging the East European economies according to its own liberal philosophy and accept state trading, target control and central price formation as alternative forms of economic organization. It was developments such as these which favoured the establishment of closer relations between the GATT and Eastern Europe.

It was not enough, though, to recognize the political desirability of improvement in East-West relations within the GATT. Was it technically feasible? There was serious disagreement among Western experts as to the possibility of finding a meaningful technical arrangement for East-West trade within the GATT framework. Some were of the opinion that no such arrangement – in harmony with GATT principles – could be worked out.⁴⁰ They maintained that East European participation in the GATT would have mostly a political character and that effective trade cooperation would continue as before outside the GATT.

According to others, effective trade cooperation between Eastern Europe and GATT members could be based exclusively on bilateral arrangements within the GATT system. These arrangements could be negotiated individually between a particular member of the GATT and the East European country in question. But arrangements along those lines could hardly have been acceptable for the GATT since they contradict the principle of multilateralism.

Finally, the optimistic attitude of still other experts was based on the assumption that the divergence in economic systems between the East and West did not constitute an insurmountable difficulty. They were convinced that meaningful institutional arrangements for East-West trade could be worked out in the GATT given a necessary minimum of the will to cooperate.⁴¹

In the view of the GATT Secretariat the problem of relations with Eastern Europe should be approached 'gradually and realistically'.⁴² The main question became the choice of the legal framework on which future membership of the centrally-planned economies in the GATT should be based.

There were two options left. First, one could introduce into the General Agreement some general provisions on target-controlled state trading along the lines of the American 'Suggested Charter'. Second, one could opt rather for a country-by-country approach, working out arrangements for particular state-trading systems in the GATT. It was the second approach that won support.

The preference for a country-by-country approach is understandable in the context of the long-term objectives that the West expected to

achieve by allowing the East Europeans to enter the GATT. They hoped to induce the centrally-planned economies to decentralize. It was rightly held that inclusion in the GATT of general provisions referring to centralized state-trading systems would tend to discourage these systems from decentralization. It would also have meant an explicit modification of the GATT philosophy, compromising GATT liberalism to the advantage of economic centralism. The country-by-country arrangement, on the other hand, was to be based on silent recognition of the special status of the target-protected, state-trading system in the GATT and of the provisory character of these arrangements.

The failure to find any uniform solution for the East European countries in the GATT was also due to the considerable differences to be found among foreign trade systems. The country-by-country approach was also consistent with Western preference for diversification of commercial policy towards Eastern Europe. It facilitated the application of double standards during the negotiations for accession, making adherence to the General Agreement easier for some East European countries than for the others.

Political considerations aside, participation of the East European countries in the GATT was also expected to bring commercial advantages to the West. The GATT could provide a framework for negotiating reciprocity arrangements with Eastern Europe, assure some new market openings for Western products and find a solution for the problem of non-discrimination both in East-West trade and in the context of CMEA commercial relations. Accession of some Eastern European countries to the GATT could also provide a unique opportunity for agreement on codes of conduct in commercial matters, especially on issues such as dumping, market disruption and exchange of information on trade.

This economic viewpoint acquired particular importance from the mid-1960s on, when American supremacy in the General Agreement had been challenged as Western Europe began to have more weight in the GATT. West Europeans were naturally more concerned with the commercial consequences of the East European presence in the GATT due to the relatively large volume of trade between the centrally-planned economies and Western Europe. Whereas West Germany, Britain, Italy and France alone accounted for more than 60 per cent of East-West trade in the late 1960s, the United States contribution to East-West trade was very low.⁴³

SUMMARY AND CONCLUSIONS

Although the Soviets preached and practised multilateralism and non-discrimination before World War II, they refused the principles of

multilateral trade and its institutions (ITO, the GATT, the IMF) in the post-war period. At that stage East Europeans feared that the Western plan for post-war economic relations, promoting freer trade and better investment opportunities, would result in United States world domination and constitute a threat to the Communist influence in Eastern Europe. It was mostly on these grounds that they refused to participate in the system.

The change in the East European attitude towards the principles of liberal trading such as non-discrimination and multilateralism occurred in the mid-1950s. Generally speaking, it resulted from two important developments: on the one hand, it became apparent to the East European countries that their economic objectives (such as industrialization and raising the standard of living) were at odds with their policy of economic separatism *vis-à-vis* the West; and, on the other hand, now that the bipolar East-West structure of world relations was an established fact, participation in the multilateral trading system seemed to communist leaders to hold fewer political risks. This led the East-European governments to favour a long-term policy for trade expansion with the Western industrialized countries. Conversion to principles of multilateral trade was thus not only a tactical adjustment; it meant the modification of East European strategy towards East-West economic cooperation.

This important evolution made even more apparent the East-West controversy on the structure of institutions regulating international trade. From the viewpoint of Eastern Europe as a bloc the GATT of the late 1950s was not a satisfactory arrangement. Being a traders' forum isolated from the political environment, the GATT was an organization in which a country's influence was positively related to its importance as a trader. The Soviet Union – a leading political and military power with considerably less significance as a trader – would have preferred to replace the GATT by a comprehensive trade organization responsive to political pressure, based on universal membership, and having a wider range of competence. In respect to these points, therefore, *rapprochement* between the Eastern bloc and the GATT is to be interpreted as a tactical adjustment intended to solve some of the practical problems of East-West commerce: reduction of barriers to trade; removal of discrimination; need of a code of conduct and of a multilateral forum for discussion; and, supervision of developments in trade.

The initial attitude of the GATT towards relations with the centrally-planned economies followed the principles of United States commercial policy towards Eastern Europe. That policy was based on preferential treatment of some East European countries, mostly for political reasons. The relations of the GATT with the East European countries were expected to develop gradually and on a country-by-country basis. The devices of centralized economic management, such as target trade

control, and central price formation, were recognized as exceptionally acceptable under the General Agreement. In a longer perspective, however, the GATT was expected to sway some of the East European systems towards decentralization and facilitate their integration into the Western economic order. In that sense the GATT was originally supposed to provide an adequate framework for implementation of the United States' commercial policy towards Eastern Europe.

The situation changed considerably in the mid-1960s when the European Community began to acquire more importance within the GATT framework. Being more economically than politically minded in their *Ostpolitik* (as opposed to Washington), the European Community's members wanted East Europeans to pay for a 'ticket of admission' to the GATT in commercial rather than political terms.

NOTES AND REFERENCES

1. The East European countries have participated in the world-wide system of economic institutions for more than ten years. On the regional level, modest efforts have been made to establish closer contacts between Eastern Europe and Western economic groupings such as the European Community, the European Free Trade Association (EFTA) and the OECD. On the world level, Yugoslavia and Romania acceded to the IMF and World Bank, while five centrally-planned economies now participate in the GATT.
2. During the course of the Bretton Woods Conference there was no indication that the Soviets would refuse to participate in the IMF and in the World Bank. See Raymond F. Mikesell, 'Negotiating at Bretton Woods, 1944', in Raymond Dennett and Joseph Jonson (eds), *Negotiating with the Russians* (Boston: Princeton University Press, for the World Peace Foundation, 1951) pp. 112–16.
3. *Suggested Charter for an International Trade Organization of the United Nations*, US Department of State Publication No. 2598, Commercial Policy Series No. 93 (1946), p.iii.
4. Alexander Gerschenkron, 'Russia and the International Trade Organization', *American Economic Review*, Manasha, Wisconsin, March 1947, p. 625.
5. Negotiators agreed that specific rules referring to complete state monopoly of foreign trade were to be introduced once an opportunity for negotiations with a country maintaining such a monopoly should occur. See: Preparatory Committee at the International Conference on Trade and Employment, *verbatim*, E/PC/T/C II/ST/PV/1, ECOSOC, London: November 1946, p. 28; and, Preparatory Committee of the United Nations Conference on Trade and Employment, E/PC/T 160, ECOSOC, Havana, August 1947, p. 8.
6. This idea is widely represented in Soviet literature. According to Soviet sources, the acceptance of the Marshall Plan would force the European governments 'to be reduced to the status of obedient puppets of the American monopolies'. See, Eugen Varga, 'The Marshall Plan and the Working Class', *New Times*, Moscow, No. 14, 1948, pp. 1–3. In the opinion of Varga, an eminent Soviet economist, the American desire for 'multilateral trade, the removal of limitations on trade tariff barriers and quotas, and the free flow of capital through the world' was dictated by the American will to dominate the world. See

also Varga, 'The Marshall Plan and the Approaching Economic Crisis in America', *New Times*, No. 39, 1947, pp. 5-7.

7. *Ibid.*, pp. 5-7.

8. Paul Baran, 'Comments in Discussion on the Economy of the USSR', *American Economic Review*, March 1947, p. 648.

9. Ernst P. Penrose, *Economic Planning for the Peace* (Princeton: Princeton University Press, 1953) p. 112.

10. Third Session of the United Nations General Assembly. *Official Records*, United Nations General Assembly, Third Session, Second Committee, Paris, 1949, pp. 154-205.

11. *Ibid.*, pp. 154-60.

12. *Official Records*, United Nations General Assembly, Third Session, Paris, 1949, Pt I, pp. 594-6.

13. *Ibid.*, p. 595.

14. Karin Kock, *International Trade Policy and the GATT* (Stockholm: Almqvist & Wiksell, 1969) p. 191.

15. *Official Records*, United Nations General Assembly, Third Session, Paris, 1949, Pt I, p. 599.

16. *Official Records*, ECOSOC, Twentieth Session, New York, July 1955, p. 77.

17. Gerard and Victoria Curzon rightly noted in their recent study: 'post-war trade liberalization has been a beneficial exercise for America's trade partners, and (. . .) if any country could be said to have "lost" within our given time-horizon, it was the United States itself.' See Gerard and Victoria Curzon, 'The Management of Trade Relations in the GATT', in Andrew Shonfield (ed.), *International Economic Relations of the Western World 1959-1971* (London: Oxford University Press, for the Royal Institute of International Affairs, 1976) p. 200.

18. Oskar Lange, *Papers in Economics and Sociology* (Warsaw: Państwowe Wydawnictwo Naukowe, 1970) p. 54.

19. *Official Records*, ECOSOC, Twentieth Session, New York, July 1955, p. 77.

20. Richard Cooper, 'Trade Policy is Foreign Policy', *Foreign Policy*, Washington, Winter 1972-73, pp. 18-21.

21. The East European criticism of the Bretton Woods institutions is included in: *Official Records*, United Nations General Assembly, Third Session, Second Committee, Paris, 1949, pp. 158 and 293-4.

22. *Official Records*, ECOSOC, Twentieth Session, New York, July 1955, p. 77.

23. See Havana Charter, Article 86. The provisions of the Article permitted the belief that the ITO would be more dependent on the United Nations political organs than was the IMF and the World Bank.

24. In Soviet opinion, one of the important disadvantages of the OTC was its close link with the GATT. They felt this would result in ignoring the problems of the developing countries and those of the state-trading economies. Moreover, the Soviets feared that the future relations of the OTC with the United Nations would be established along the same lines as in the case of the IMF and the World Bank - which the Soviet Union judged unsatisfactory. For more extensive analysis see: Georges Fischer, 'Organization de Cooperation Commerciale', *Annuaire Français de Droit International*, Paris, 1955, p. 421.

25. *Report of the Group of Experts Appointed under Resolution 919 XXXIV of the ECOSOC*, E/3756, (Geneva: UNCTAD, 1963) pp. 96–9.
26. The organization was expected to conduct a broad range of activities – including the formulation of recommendations for promoting international trade, a discussion on prices for raw materials and industrial products and supply of industrial equipment to the developing countries. Moreover, the agency should go forward with the work of formulating a legal framework for international trade and could make recommendations for the conclusion of long-term multilateral trade agreements. *Ibid.*, pp. 96–9.
27. General Assembly resolution 1995 (XIX) of 30 December 1964, Paras 30–1.
28. *Question of the Establishment of a Comprehensive Trade Organization*, TD/6/535 (Geneva: UNCTAD, 1974) and *Interdependence of Problems of Trade, Development, Finance and the International Monetary System*, TD/B/459 (Geneva: UNCTAD, 1973).
29. Gerard Curzon and Victoria Curzon, 'GATT: Traders' Club', in Robert Cox *et al.* (eds), *The Anatomy of Influence* (New Haven and London: Yale University Press, 1973) pp. 298–333.
30. There is substantial literature on this matter. See Kock, *International Trade Policy*, *op. cit.*, pp. 192–202.
31. In 1958 the following GATT countries did maintain bilateral agreements providing for MFN treatment to Poland: Austria, Brazil, Canada, Chile, Dominican Republic, Greece, Haiti, India, Indonesia, Japan, Malaysia, New Zealand, Peru, South Africa, the United States, Uruguay and West Germany. Canada applied MFN treatment on the basis of a pre-war treaty. MFN tariff treatment was applied to Poland *de facto* by West Germany and Japan. The above information, indicated in a document of the Polish Ministry of Foreign Trade, has been quoted by Jan Woźnowski, *Polska w GATT* (Warsaw: Państwowe Wydawnictwo Ekonomiczne, 1974) p. 62.
32. Tadeusz Szczurski, *Zasada największego uprzywilejowania w GATT* (Warsaw: Polska Izba Handlu Zagranicznego, 1970) pp. 93–8.
33. Woźnowski, *Polska w GATT*, *op. cit.*, p. 69. The same study contains an extensive and well done analysis of relations between Poland and the GATT.
34. Ranking of traders according to their share in the world's imports in 1967:

- (1) European Community, (2) United States, (3) West Germany, (4) United Kingdom, (5) France, (6) Japan, (7) Canada, (8) Italy, (9) Soviet Union, (10) Netherlands, (. . .) (17) German Democratic Republic, (18) Czechoslovakia, (19) Poland, (. . .) (26) Hungary, (27) Yugoslavia, (28) Bulgaria, (30) Romania, (. . .) (41) Cuba.

Robert Cox and Harold K. Jacobson indicated the following ranking of countries according to their power in international system:

- (1) United States, (2) Soviet Union, (3) France, (4) China, (5) Japan, (6) United Kingdom, (. . .) (18) Yugoslavia, (. . .) (22) Poland, (. . .) (24) Czechoslovakia, (. . .) (26) German Democratic Republic, (. . .) (36) Cuba.

Note the difference in the rank of the Soviet Union among the traders and among the powers.

Ranking of traders according to import statistics of *Yearbook of International Trade Statistics* 1970–71 (New York: United Nations, 1973). Intra-CMEA trade converted into dollars at official exchange rate 0.90 RB \$.

For ranking of countries according to their power see: Cox *et al.* (eds), *op. cit.*, pp. 37–58.

35. Dependence of the East European countries on East-West trade (1965–67) is as follows: Bulgaria–12.5 per cent; Hungary–11.6 per cent; Romania–9.6 per cent; Czechoslovakia–9.0 per cent; German Democratic Republic –8.6 per cent; Poland–6.7 per cent; and the Soviet Union–1.5 per cent. Dependence on East-West trade was calculated according to the following formula:

$$\left[a = \frac{X + M}{GMP} \cdot 100\% \right]$$

and where:

X signifies value of country's export to the West,

M value of country's imports from the West,

GMP gross material product which may be defined as gross national product minus the non-productive services.

Own calculation; GMP data in US dollars estimated on the basis of the ECE's statistics; *Economic Survey of Europe, part I: Structural Trends and Prospects in the European Economies* (New York: United Nations, 1970) p. 150.

36. No official contacts between the Soviet Government and the GATT Secretariat took place in relation to the eventual participation of the Soviet Union in the GATT. This point had been made, however, in unofficial conversations in Geneva in the late 1960s.

37. Article of the Soviet Vice-Prime Minister, Anastas Mikoyan, on the GATT was published in the West German *Handelsblatt*, 20 May 1960.

38. I. Niesnanov, 'GATT', in *Bol šaja Sovjetskaja Enciclopedia* (Moscow: 1971) Vol. 6, p. 221.

39. John P. de Gara, *Trade Relations between the Common Market and the Eastern Bloc* (Bruges: De Tempel, 1964) pp. 19–28.

40. K. R. Gupta, 'GATT and State Trading', *Economia Internazionale*, Rome, February 1967, p. 59.

41. That attitude, to which the author of the present study also subscribes, is inspired by numerous discussions which took place on that issue before World War II and in the post-war period. For the discussions in the League of Nations see G. W. Wickersham, *Report of Sub-Committee on the Most-Favoured-Nation Clause* (Geneva: League of Nations, 1927).

42. Eric Wyndham White, 'International Trade: Challenge and Response', an Address at the Fletcher School of Law and Diplomacy (Geneva: GATT Secretariat, 1959) p. 19.

43. In 1969, the share of East European imports in total imports amounted to: 3.7 per cent for West Germany, 4.0 per cent for Britain; 5.6 per cent for Italy; 2.6 per cent for France; and about 0.7 per cent for the United States. Note that East-West trade accounted for a smaller share of total trade in the West than in the

East. In 1969, Poland was purchasing 26 per cent of her imports in the Western developed economies; Romania, 40 per cent; Hungary, 27 per cent; and Czechoslovakia, 25 per cent. These figures explain why the East European motives underlying accession to the GATT were more economic than political, whereas the Western attitude towards accession of the East European economies to the GATT was determined largely by political factors.

Relations of the East European Countries with the GATT

Four patterns of relations have been established between Eastern Europe and the members of the GATT. First, there is the case of Czechoslovakia. Czechoslovakia did not become a target-protected, state-trading country until it was already in the GATT. Second, there is the example of Yugoslavia. She approached the GATT after removing her target protection and acceded to the General Agreement, claiming that her foreign trade system was in full conformity with the principles of the GATT. Third, there are the cases of Poland and Romania, where the GATT accommodated itself to the foreign trade systems in the two countries. Finally, Hungary offers an example where the country's accommodation and the GATT's accommodation met halfway.

PRECURSORY EXPERIENCE

CZECHOSLOVAKIA IN THE GATT

The case of Czechoslovakia and the GATT is relatively well documented.¹ The following discussion will mainly deal with the way the Czechoslovak experience influenced the elaboration of GATT mechanisms for dealing with the state-trading systems.

Czechoslovakia is an original member of the GATT. At the time the General Agreement was drafted, Czechoslovakia was not yet a target-protected economy. It was, however, the new socialist government of Czechoslovakia which, in March 1948, gave its assent to the GATT. Although Czechoslovakia's legal situation in the GATT took shape before the introduction of the target-protected state-trading system, no renegotiation of Czechoslovakia's terms of membership was conducted in order to adjust to these changes.

Czechoslovakia continued to grant tariff concessions to the GATT countries although this was no longer her essential instrument for trade control. This met with protest from the United States – the only GATT country to recognize the situation as fictitious.² The American protest conjugated with Czechoslovak criticism of American discriminatory trade policy against Eastern Europe and resulted in a series of disputes between the two countries in the GATT. The Contracting Parties recognized that the disputes were due to 'exceptional circumstances of a kind different from those contemplated under the General Agreement'.³ Given the political overtones of the controversy and its apparent insolubility, the United States renounced their relations with Czechoslovakia under the General Agreement. No other countries followed the American example, although a majority of them applied discriminatory tariffs, quotas and licensing against trade with Czechoslovakia during the Cold War.

Three technical issues concerning the participation of target-protected and state-trading systems in the GATT came up with reference to Czechoslovakia. First, it was felt that the GATT's criteria on dumping could not provide a fully satisfactory standard for relations with Czechoslovakia. The interpretative note appended to the GATT dumping article and introducing additional criteria on dumping was conceived as a result of Czechoslovakia's presence in the GATT. Secondly, after her withdrawal from the IMF, a waiver was granted to Czechoslovakia releasing her from the obligation of entering into special exchange agreements. It should be noted, however, that a similar solution had been previously adopted for some market economies and thus could not be considered a specific concession to the state-trading systems. Finally, efforts to reconsider the reciprocity arrangements between target-protected Czechoslovakia and the essentially tariff-protected GATT countries were made in discussions preceding the Kennedy Round negotiations. Since reduction of Czechoslovak customs tariffs was not likely to be considered by GATT partners as a sufficient concession, Czechoslovakia decided to advance a new proposal. Apart from custom duties, Czechoslovakia suggested increasing imports from the GATT countries by a given percentage, say 30 per cent, for five years, in exchange for the removal of discriminatory quantitative restrictions on Czechoslovak exports to market economies. This proposal, which follows the lines of the Polish solution for participation in the Kennedy Round, was not accepted by the most important Western partners. Besides, Czechoslovakia soon realized that, as regards tariffs, no more was to be obtained from the Kennedy Round than could be obtained on the basis of MFN treatment from other countries' negotiations.

Thus, aside from the dumping formula, Czechoslovak participation in the GATT did not result in any contribution to the development of

technical arrangements for target-protected, state-trading systems in the General Agreement. Czechoslovakia's participation in the GATT during the Cold War has to be interpreted as an effort to maintain traditional contacts between Czech industries and the West. Despite GATT membership, Czechoslovakia was treated in the West much the same as those centrally-planned economies outside the GATT. However, not very much was required of Czechoslovakia during her presence in the GATT. Western states particularly interested in developing commercial relations with Czechoslovakia preferred to enter into bilateral commercial agreements rather than to rely on the GATT relationship.

YUGOSLAVIA'S PATH TO THE GATT

From the moment of its break with the East European bloc (1948), Yugoslavia conducted an independent foreign policy, trying to find its way in a world marked by East-West polarity. At the same time, Yugoslavia progressively engaged in the decentralization process, meant to establish a so-called market socialism with worker management of the economic units. The first of these factors heralded the removal of political obstacles, which for years kept other centrally-planned economies away from the GATT. The second permitted Yugoslavia to adapt increasingly to the GATT system and finally to accede to the GATT as a tariff-protected country maintaining occasional state trading.

During the Cold-War period Yugoslavia enjoyed special relationships with the United States. Unlike other East European countries, Yugoslavia was not subject to the provisions of the Trade Agreement Extension Act (1951), which deprived Communist or Communist-dominated countries of the MFN treatment. In addition, it benefited from important American loans and grants, which the United States regarded basically as political assistance.

When Yugoslavia first approached the GATT in 1950 and asked for observer status, it was a state-trading economy maintaining target protection.⁴ Nevertheless Yugoslavia's *rapprochement* with the GATT coincided with its move away from the domestic model of a centrally-planned economy and an increase in trade with the West. In spite of the steady pace of decentralization, even in 1958 Yugoslavia was not yet able to assume the obligations of full membership in the GATT.⁵ Instead it established special relations with the GATT countries often referred to as 'association'. This meant, first of all, that commercial relations between Yugoslavia and the GATT countries would be conducted in conformity with the rules of the GATT to the extent possible under the Yugoslav economic system.⁶ It meant also that Yugoslavia was invited to participate in Sessions and subsidiary bodies

of the GATT. The arrangement was conceived as a test of the possibility of developing trade relations with Yugoslavia on GATT terms and was to provide an incentive for progress towards full application of the General Agreement by Yugoslavia.

During the three years of association, which preceded provisional accession to the GATT in 1962, Yugoslavia continued to decentralize its economic and foreign trade system. The introduction of tariffs, abolition of multiple exchange rates, moves towards multilateralism, and simplification of trade control, brought the Yugoslav economic and foreign trade system closer to the requirements of the General Agreement.⁷ Some important difficulties arose, however, with introduction of the definitive customs tariff. Mainly due to disparities between Yugoslav and world prices, Yugoslavia was not able to bring its tariffs to levels acceptable for negotiations in the GATT (in some cases a 300 per cent tariff was required). Since Yugoslavia was not able to enter the GATT by paying for its 'ticket of admission' through tariff reductions, agreement was reached on provisional accession (1962).⁸ Under the terms of provisional accession, Yugoslavia enjoyed tariff concessions from the GATT countries with the exception of the United States.⁹ The United States Congress, when adopting the Trade Expansion Act (1962), broadened the provisions referring to 'communist states', so that the law also had to be applied to Yugoslavia. That decision reflected some deterioration in the political relations between the United States and Yugoslavia.

The Kennedy Round gave Yugoslavia the opportunity to fulfil its obligations in tariff negotiations. Moreover, the final agreement on the terms of full membership in the GATT was further facilitated by the broad decentralization of the Yugoslav economic system from 1962 onwards.

At the time of full accession (1966), Yugoslavia claimed to use tariffs as the only instrument of trade control under normal conditions. State trading was said to be used only as a rare exception. There existed free price formation, a unified exchange rate, and no export subsidies. Owing to the balance-of-payments situation Yugoslavia also used direct trade control, but it implemented that control in a non-discriminatory manner.

Through its accession to the GATT Yugoslavia acquired direct rights with respect to concessions among the members of the GATT and the right to vote on decisions of the contracting parties.¹⁰ This time, the United States accepted the protocol for accession and granted MFN treatment to Yugoslavia.

The importance of the Yugoslav experience in the GATT for other centrally-planned countries may be summarized as follows. First, this experience, especially in its earlier stage, provided the GATT countries with the opportunity to acquaint themselves with difficulties that would

arise in relations with target-protected, state-trading systems. Secondly, Yugoslavia's participation in the GATT provided empirical evidence that socialist economies could decentralize sufficiently to permit their membership of the GATT under the same conditions as Western market economies. Finally, Yugoslavia's road to the GATT clearly demonstrated that substantial reforms are required in order to shift from a target-protected, state-trading system to the GATT model of foreign trade and that, even under political conditions extremely favourable to decentralization, years of adjustment are necessary.

NEGOTIATING WITH STATE-TRADING COUNTRIES

POLAND AND ROMANIA

In contrast to Yugoslavia, Poland and Romania approached the GATT without adjusting their foreign trading systems to the traditional GATT pattern. Consequently, the two countries present 'special cases' of target-protected, state-trading systems admitted to the essentially liberal General Agreement.

The first informal discussions concerning Poland's participation in the General Agreement took place in 1957. Politically, the times were extremely conducive to such a move. Political and economic reforms following the events of the Polish October (1956) resulted in important modification of Western policies towards Poland. Wladyslaw Gomulka's government enjoyed preferential credit policy in the West and benefited from important deliveries of surplus farm commodities from the United States. In October 1957, Poland became an observer in the GATT and expressed its desire to join the General Agreement as a full member.

Initially, Poland considered the possibility of acceding to the GATT on a tariff basis. Propagators of economic reforms in post-October Poland expected that, with decentralization, tariffs could become an effective instrument of trade control both for Poland's trade with the West and with the CMEA countries.¹¹ Due to 'political normalization', however, and some purely economic considerations, not much progress towards economic decentralization was accomplished and Poland was obliged to abandon its project of accession to the GATT along the lines of the later Yugoslav pattern.¹²

Under these circumstances, the Polish Vice-Minister of Foreign Trade, Finciszek Modrzewski presented to the GATT a proposal based on the idea of an import commitment by Poland.¹³ It corresponded to suggestions made by the GATT Secretariat after previous consultations with the main GATT countries.

Although no official discussion on the Polish proposal took place at

that time, Poland requested full membership in March 1959. It met only with partial success. The United States, Canada, Britain and some other GATT countries considered that Poland was not yet able to assume the obligations of full membership.¹⁴ Instead, they suggested another formula for closer relations with the Polish Government.

The declaration providing for Poland's association with the GATT was issued in November 1959.¹⁵ It provided for annual review of trade relations with Poland and invited Polish participation in certain bodies of the GATT. An important weakness, however, of the declaration was the failure to define a basis for Poland's participation in the multilateral trade negotiations. Since Poland was unable to adjust her foreign trade system to the rules of the GATT, her association period, as distinguished from that of Yugoslavia, had to be a time for working out a formula permitting accommodation of the GATT to the Polish economic system.

The first opportunity for discussing a reciprocity formula arose in 1959 in reference to the Dillon Round. Poland expressed an interest in participating in these trade negotiations on the basis of a so-called minimal import commitment. The proposal, however, did not arouse much interest among the GATT countries, which were, at that time, preoccupied with more important issues,¹⁶ but it is possible that the Polish suggestion was just submitted too late. Several important members of the GATT considered that the question required more serious consideration before any decision could be taken. Finally, due to some estrangement in relations between Poland and the United States, and the small quantitative importance of Poland's trade with the GATT countries, the West was cool to the idea of having Poland at the negotiating table during the Dillon Round (1960–62).

All things considered, the period of Poland's association with the GATT up to the Kennedy Round was fruitful. One positive indirect effect of this association, however, was the eventual extension of MFN treatment to Poland by the United States. During negotiations on that issue, the Polish party was informed that closer relations between Poland and the GATT could help solve the problem.¹⁷ Immediately after the declaration of 1959 entered into force (1960), the American administration granted MFN treatment to Poland. It is worth noting that closer relations between Poland and the GATT also had a positive impact on the subsequent development of events relating to MFN status for Poland in the United States. In 1962 the MFN clause was formally withdrawn (by Congressional decision); however, the President of the United States maintained it *de facto*.¹⁸ Formal application of MFN treatment to Poland was reintroduced in March 1964 by virtue of the Foreign Assistance Act (1963).

The period of Poland's association with the GATT coincided with growth in Poland's trade with the GATT area. The expansion of Polish exports was, in certain cases, attributed to trade liberalization measures

or other actions taken in pursuance of the objectives of the declaration on association.¹⁹

Poland's interest in the Kennedy Round was warmly welcomed by the participants in the multilateral trade negotiations.²⁰ She submitted an offer of concessions (global commitment to increase imports from the GATT area by 40 per cent in five years) in exchange for expected tariff reduction and removal of the discriminatory QRs on Polish exports. However, the Polish offer did not appeal to the main negotiators. The offer was global in nature and therefore unlikely to attract the attention of any specific Western industry looking for additional market openings. In addition, the small quantitative importance of Polish trade with the GATT countries and the unusual nature of the suggested reciprocity formula were further obstacles. It would seem that the United States and the countries of the European Community were too occupied with their own problems to be concerned with the Polish issue.²¹

For Poland, the most important contribution of the Kennedy Round was the working out of some technical solutions which provided a starting-point for further negotiations on accession. During these negotiations Poland took advantage of support from the 'anti-EEC front' in the GATT (mostly the United States, Britain and Canada), which encouraged demands for elimination of the discriminatory QRs on Polish exports by the countries of the Community.²²

At no time were negotiations easy. Spokesmen often were forced to revert to informal consultations before an agreement could be reached. Also the GATT Secretariat, which considered Poland's accession to the Agreement an important step in the GATT evolution towards universality, played a significant role as mediator.

On balance, the Kennedy Round was fruitful for Poland. First, the protocol of accession was annexed to the Final Act of the Kennedy Round – and in October 1967 Poland became a full member of the General Agreement.²³ Second, Poland did take advantage of the tariff reductions agreed upon during the Kennedy Round by virtue of its MFN clause. On the other hand, due to elimination from the Kennedy Round of negotiations on agricultural products, as well as maintenance of discriminatory QRs on Polish exports, Poland's benefits were considerably reduced.

The Polish example greatly influenced Romania's relations with the GATT. Romania approached the members of the General Agreement in 1957 and was accepted as an observer. That move coincided with significant political changes in Romania. Romania was the first East European country to take advantage of the Sino-Soviet dispute and assume a larger margin of foreign policy independence in the Eastern bloc. She successfully opposed efforts to transform the CMEA into an institution of supranational planification, and in the 1956–62 period the CMEA reoriented its trade towards Western countries and undertook

new forms of economic cooperation with the industrialized countries. Participation in those international organizations, likely to contribute to the development of trade and other forms of economic relations with the West, became an integral part of this policy.

Romania undertook efforts to accede to the GATT after ten years as an observer in the General Agreement. Several factors explain the length of this initial period. The Romanian Government wished to withhold its application for accession to the GATT until negotiations with Poland had been completed. The Government rightly expected that the Polish case would provide a test case. Secondly, Romania did not have much interest in the Kennedy Round: it considered itself a developing country and quite unprepared to grant any important concessions during the multilateral trade negotiations. Finally, in the late 1950s and the early 1960s Romanian relations with the United States were far from being as good as Poland's. The United States refused to grant Romania MFN treatment, in spite of the fact that two other centrally-planned economies – Poland and Yugoslavia – benefited from the MFN clause on the American market. At that time, Romania could not expect the United States to support its accession to the GATT.

It was in July 1967 that Romania presented a formal application for accession to the General Agreement.²⁴ Like Poland, Romania intended to join the GATT while maintaining target control and state trading. Considering itself a less-developed country, however, Romania expected to obtain more advantageous terms of accession than Poland.

Negotiations were conducted in a very favourable political atmosphere. Romania gained considerable sympathy in the West for its independence *vis-à-vis* the Soviet Union, especially during the 1968 events in Czechoslovakia. Romania, moreover, played an important role in helping to pave the road for the relaxation of tension between the United States and China. These efforts were kept in mind by the United States Nixon Administration when dealing with the problem of granting MFN treatment to Romania.²⁵ Due to their legislation, however, which forbade the granting of MFN treatment to Romania, the United States were initially obliged to invoke Article XXXV and abstain from negotiations for Romania's accession.

The difficulties that cropped up during the negotiations for accession were similar to those in the Polish case: much time was spent discussing the problem of reciprocity, non-discrimination and safeguard arrangements. Foremost among the important economic issues discussed was the elimination of discriminatory QRs on Romanian exports to some West European countries.

Romania's accession to the GATT took effect in November 1971 and coincided with her participation in the IMF and the World Bank. These developments are consistent with Romania's efforts to strengthen her links with the West.

HUNGARY

Hungary's initial efforts to establish contacts with the GATT were thwarted. In 1958, Hungary, following the example of Poland and Romania, applied for observer status in the GATT. After the events of 1956 in Budapest, however, the political climate was unpromising. The United States and some other GATT countries objected to the Hungarian application which had to be withdrawn. From the mid-1960s on, the Hungarians were preoccupied with the reform of their own economic system. Broadly speaking, the reform aimed at increasing the market's role in the domestic economy and in foreign trade. This was of great significance for Hungary's relations with the GATT, since it made possible partial adjustment of the Hungarian trade régime to the traditional GATT system.²⁶

In 1966 Hungary presented its second request for observer status in the GATT and was accepted. Three years later, after the introduction of some further changes in its economic system, the Hungarian Government decided to apply for full membership. This time it was well received by the United States, the European Community and other GATT countries.

Due to the tariff approach put forward by Hungary, negotiations centred first on the technical issues concerning the operation of the Hungarian tariff system, price formation and other related matters of importance for future tariff concessions. As in the case of Poland and Romania, the spokesmen of the European Community were chiefly concerned with the technical and economic issues, and the Hungarian negotiators were frequently obliged to resort to informal discussions with the Community representatives before agreement could be reached.

The final success of the negotiations was certainly due to the political sympathy of the Western governments towards Hungarian efforts at economic decentralization. This factor constituted the background of many technical discussions.

The United States supported Hungary's accession to the GATT. As in the case of Romania, however, the American delegation was obliged to invoke Article XXXV and could not establish relations with Hungary as a GATT partner.

In 1973 Hungary conducted successful tariff negotiations with the GATT partners and Hungary's accession to the GATT took effect in September 1973.

Among the other centrally-planned economies, Bulgaria has shown greatest interest in the General Agreement. She has been an observer in the GATT since 1967 and is participating in the Tokyo Round negotiations.

SUMMARY AND CONCLUSIONS

The diversity of Eastern Europe's foreign trading systems and the shifts in political climate which happened to influence the evolution of specific East-GATT negotiations explain why, in each case, East European participation in the GATT is regulated by different terms.

Among the five countries admitted to the GATT, Poland, Romania and Hungary provide the most interesting (and revealing) cases. Czechoslovakia's entrance provided little opportunity for reconsidering the technicalities of East-West trade cooperation. Yugoslavia, although a centrally-planned economy, entered the GATT claiming tariff protection, internal competition and the absence (as a rule) of state trading.

It is Poland's *rapprochement* with the GATT that provided a first opportunity to negotiate some concrete technical arrangements for target-protected, state-trading systems in the essentially liberal GATT. The Polish experience influenced the Romanian and Hungarian negotiations, providing both a political precedent as the East European newcomer and an example for technical arrangements. It was Romania that followed the Polish pattern most closely.

The Hungarian formula of accession was made possible by the broad decentralization of the Hungarian economic system in 1968. The terms of the Hungarian participation, as compared with those of Poland and Romania, may be considered as further progress in the GATT's pragmatic approach to trade relations with the centrally-planned economies of Eastern Europe.

NOTES AND REFERENCES

1. See, for example, Gerard Curzon, *Multilateral Commercial Diplomacy: an Examination of the Impact of the General Agreement on Tariffs and Trade on National Commercial Policies and Techniques* (London: Michael Joseph, 1965) pp. 298-301.
2. *Basic Instruments and Selected Documents* (Geneva: GATT Secretariat, 1952) Vol. II, p. 36. Hereafter cited as *GATT Basic Instruments*.
3. *Ibid.*, p. 36. The United States Congress accepted the Trade Agreement Extension Act requiring withdrawal of MFN treatment in trade with the 'communist-dominated countries'.
4. This *rapprochement* with the GATT (at that time an essentially Western institution of trade cooperation) corresponded to Yugoslavia's membership in the IMF and the World Bank.
5. GATT Doc. L/870, October 1958.
6. For the GATT countries which signed the declaration establishing relations with Yugoslavia, see *GATT Basic Instruments*, 8th Supplement, 1960, p. 18.
7. Evolution of the Yugoslav foreign trade system is discussed by Harriet

Matejka, 'Foreign Trade Systems', in Hans-H. Hohman, Michael Kaser, Kare Thalheim (eds), *The New Economic Systems of Eastern Europe* (London: Oxford University Press, 1975) pp. 468–73.

8. For the declaration on provisional accession, see GATT, *Basic Instruments* 11th Supplement 1962, p. 50. It applied only to those GATT countries that signed the declaration.

9. Yugoslavia did not acquire direct rights with respect to those concessions, that is, it could not demand compensation for tariff concessions withdrawn by another contracting party.

10. Report of the Working Party on Accession is included in GATT *Basic Instruments*, 14th supplement, 1966, pp. 49–59.

11. GATT Doc. MGT/81/58, August 1958, p. 9; and GATT Doc. MGT/81/58, Add. 1, October 1958, p. 1.

12. A Polish source indicates that one of the main difficulties in introducing tariffs as effective instruments of trade control was the necessity of a *de facto* devaluation. See Zdzisław Rurarz, 'Reviewer's Note on "Polska w GATT" by Jan Woźnowski', *Sprawy Międzynarodowe*, Warsaw, January 1975, p. 141.

13. GATT Doc. Spec. 102/58, April 1958, p. 4. Minister Modrzewski was one of the initiators of the Polish *rapprochement* with the GATT.

14. In Polish literature, there is a tendency to attribute the 1959 refusal to political factors. See Wojciech Morawiecki, 'Some Particular Aspects of Poland's Membership in International Organizations (UN, ICAO, GATT)', *The Polish Yearbook of International Law*, Warsaw, Vol. II, 1968–69, p. 18.

15. Within the working party concerned with the issue, the European Community and the United States strongly supported the idea of declaration without insisting much on technical matters. Great Britain seemed to be particularly concerned with economic aspects of relations with Poland and stressed the question of reciprocity. GATT, Doc. SR/15/12, November 1959. For the text of the declaration, see GATT, *Basic Instruments*, 8th Supplement, 1960, pp. 11–14.

16. Specific advantages and disadvantages of the global commitment as compared with a commodity are discussed in Chapter 3.

17. Rurarz, *op.cit.*, p. 141.

18. *Ibid.*, p. 141.

19. GATT *Basic Instruments*, 11th Supplement, 1963, p. 73.

20. Bohdan Laczkowski, 'Poland's Participation in the Kennedy Round', in Frans Altling von Geusau (ed.), *Economic Relations after the Kennedy Round* (Tinburg: Sijthoff-Leyden, 1967) pp. 83–93; and GATT Doc. TN/64/NTB/15, April 1964, p. 5.

21. The Polish offer of concessions was withdrawn on the grounds that some GATT countries refused to remove discriminatory QRs on Polish exports.

22. Negotiations on Poland's accession to the GATT were of interest to all important GATT member countries. The following countries became participants of the working party: Australia, Austria, Belgium, Canada, Czechoslovakia, France, Holland, Great Britain, India, Italy, Israel, Japan, Luxemburg, Nigeria, Pakistan, Poland, Sweden, United States, West Germany and representatives of the Commission and the Council of the European Community.

23. The technical arrangements for Poland's, Romania's and Hungary's membership in the GATT are discussed in Chapter 5.

24. GATT Doc. L/3050, August 1968, p. 1.
25. *International Herald Tribune*, Paris, 26 July 1971.
26. Maciej Kostecki, 'Hungary and GATT', *Journal of World Trade Law*, Twickenham, July–August 1974, pp. 401–19.

State-trading Systems and the GATT Framework

The General Agreement was created for market economies and essentially private-enterprise economies. It was unlikely, therefore, to provide an adequate framework to deal with centralized economies and essentially state-enterprise economies. Both the application of its principles and the clauses most appropriate to state trading seemed likely to raise problems. This chapter reviews GATT rules on non-discrimination, reciprocity, trade control, state trading and safeguard action, and considers the difficulties to be expected in applying them to state-enterprise economies.

PRINCIPLES OF THE GATT

NON-DISCRIMINATION

The general principles which guide the GATT and underlie the detailed rules of its structure are comparatively few in number. They may be stated as follows: non-discrimination, reciprocity, tariff (the main protecting element), adaptability, and consultation.

Non-discrimination is the central concept of the General Agreement. It is first expressed in the famous most-favoured-nation clause (Article I), which requires that: 'any advantage, favor, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territory of all other contracting parties.' The provision is of an all-inclusive nature since it refers not only to customs duties and charges, but also to all rules and formalities concerning imports and exports. No matter how a government regulates its foreign trade, it may not, in principle, discriminate as to the origin or destination of traded goods. Nothing in the formulation of this principle precludes its application to the state-trading system.

In so far as the principle of non-discrimination applies to tariffs, it is subject to several major exceptions. Most important among these are two forms of regional integration – namely the customs union and the free-trading area.¹ Although technically incompatible with the principle of non-discrimination, regional integration is considered a movement towards the GATT's final goal of freer trade.

Another exception, in practice particularly relevant to political discrimination, is set forth in Article XXI of the General Agreement. It provides that a GATT member can take any action it considers necessary to maintain its security.² The Western strategic embargo on exports to Czechoslovakia during the Cold War was often justified under these provisions.

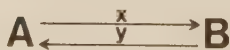
An important consequence of the principle of non-discrimination is that any modification of concessions agreed upon among certain GATT countries must be accorded to all other GATT countries.³ Taken in that sense, non-discrimination may be said to clash with the principle of reciprocity discussed below. Like many other GATT members, the state-trading countries in the GATT have profited from some tariff reductions, often without according any reciprocal concessions.

So much of GATT behaviour is motivated by the principle of non-discrimination that it would have to play a major role in any special arrangements made to allow the participation of state-trading systems in the GATT. A correct understanding of the conditions under which non-discrimination may be meaningfully applied to state-trading economies requires a more detailed discussion, which will be presented later. Difficulties may be expected in the application of that concept to the state-trading systems in view of their use of direct controls.

RECIPROCITY

'Reciprocity' (unlike 'non-discrimination') is not written in capital letters in the General Agreement but it is certainly a motivating principle in many GATT assaults on trade barriers.⁴

Reciprocity is an exchange of concessions during commercial negotiations, where every government aims at maximizing its gains from trade cooperation. Reciprocity is a four-element relation.



Government A grants concession x to government or group of governments B. Since x is of value to B, government A may ask for and obtain reciprocal concession y from B.⁵ If A is a rational negotiator, he will refuse to accept a situation where the costs of granting concession x exceed the benefits of receiving concession y . Thus, trade cooperation

between A and B can make sense only when benefits are at least equal to costs for each party in the transaction. Those benefits may exceed costs mostly for two reasons: that partners take advantage of gains from freer trade and that partners use divergent criteria to evaluate costs and benefits when exchanging concessions.

Several arguments may be advanced to explain the importance of reciprocity in the GATT negotiations. Let us briefly examine each of them in turn. The balance-of-payments argument and the closely related employment argument for reciprocity run as follows.

Under a fixed exchange rate, if balancing of the trade account is a government policy, concessions by country A that result in an expansion of exports for country B should be exchanged against equivalent concessions from country B resulting in export expansion for country A. Based on that argument, reciprocity between A and B should assure a dollar for exports against a dollar for imports.⁶ In respect to employment, reciprocity offers the possibility of balancing the employment-reducing effects of import openings with the employment-creating effects of export openings.

Ernest Preeg, an American diplomat, referring to the Kennedy Round and preceding negotiations, observed that countries tended to strike a rough balance in value terms between the estimated increases in imports and the forecast rise in exports to result from the concessions.⁷ It could be added that in many cases minimum standards of reciprocity depended not so much on the balance in incremental trade flows (as Preeg suggests) but on the balance in incremental and existing flows. Evidence to support that claim may be found in the numerous discussions in the GATT forum between the surplus and the deficit countries.⁸

The balance-of-payments criteria provided the most widely used standard of reciprocity in the Kennedy Round. As Preeg remarked, reciprocity was measured there in terms of expected increases in trade flows, trade volume offered for concessions, loss of collected customs duties or average depth of tariff cuts.⁹ It was the first method that was most widely used by negotiators both in the GATT forum and at home. Gerard and Victoria Curzon, both economists at the University of Geneva, rightly noted that all negotiators return home with their own calculations providing that they have succeeded in negotiating an advantageous trade bargain. They tended to show that the export opportunities they obtained were greater than the import openings they conceded. Of course, this logically cannot be true for all of them at the same time.¹⁰ Whereas the balance of payments provided the most forceful reciprocity argument under the relatively fixed exchange-rate system, it is doubtful whether the approach remains fully valid for the present world of flexible exchange rates. Indeed, under flexible exchange rates and abstracting from the complications of capital movements, the

equality in changes in export and import values will be automatically ensured by the changes in the exchange rate. Floating exchange rates raise, thus, important issues in respect of arguments for reciprocity in the Tokyo Round. This necessitates coping with problems of employment, inflation, and complex effects that changes in the exchange rates may have on import-competing industries.¹¹

Even though the balance-of-payments argument has lost a lot of its pertinence for the market economies, it is still valid for the centrally-planned foreign trade systems, where exchange rates do not provide an essential means of dealing with balance-of-payments disequilibria (see Chapter 3). Consequently, the problem of East-West trade reciprocity could logically be expected to gain in relative importance in the multilateral trade negotiations.

Moreover, since the balance-of-payments argument is particularly valid for East-West trade, partly due to a simple pattern of East-West capital movements, the measuring of statistical reciprocity by means of trade flows remains convincing (Chapter 6).

Economic theory also advances a terms-of-trade argument for reciprocity, which runs as follows. When the country's protection involves the exploitation of monopoly-monopsony power on the international market and assuming this is tied to real income maximization, the country would not unilaterally abandon protection in favour of freer trade. In that case, a reciprocal reduction of trade barriers, effecting no change in terms of trade, may be the only path to freer trade.¹² This argument is not of much interest in the context of the GATT. Where some monopoly-monopsony power exists in international markets (for example, territorial monopoly of raw materials) tariffs are rarely used to exercise it. Neither is the argument of much relevance for East European members of the GATT, since they have little or no monopoly position in the world trade.¹³

Protectionist policies may as well result from a 'preference for economic balance' (to use the expression of Robert Mundell, the Canadian economist), meaning a country's desire to maintain a certain equilibrium between the industrial and agricultural sectors of its economy. Industrial protectionism is characteristic of socialist countries with relatively important agricultural sectors and aiming at further industrialization. Agricultural protectionism is a major common policy of industrialized countries where governments show special concern for agricultural production.¹⁴ This line of thought provides an elegant framework for arguments in favour of East European requests for removal of West European discriminatory QRs. Since these quotas are most often imposed on Eastern Europe's agricultural exports, new market openings for Western industrial products in centrally-planned economies could be interpreted in the same spirit, as contrary to Eastern Europe's desire for industrialization. Such being the case, Eastern

Europe could quite justly require – in exchange for openings to Western industrial products – reciprocal concessions improving the access of its food products to West European countries.¹⁵

A useful concept for explaining the decision-making relating to reciprocity arrangements is the mechanism of ‘pressure and support’ shaping commercial policy. The structure of a country’s protection may be looked upon as an expression of domestic bargaining among industries. The mechanism of interrelation of the mechanism of ‘pressure and support’ through reciprocity is schematically presented in Figure 3.1.

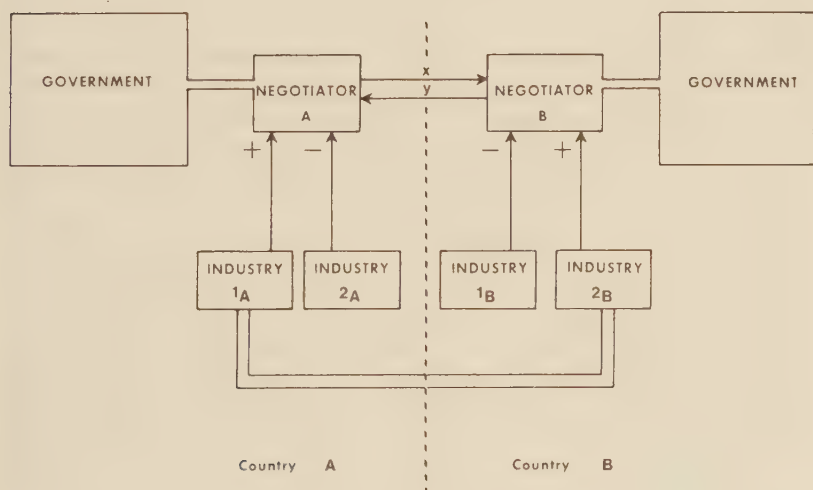


FIGURE 3.1
Internal Pressure and Support in Commercial Policy Bargains

Industry 1_A desires market openings (concession y) in country B. That concession threatens the interests of industry 1_B . Consequently, industry 1_B puts pressure on its government not to grant concession y to country A. (Government B has to take into account the balance of political pressure and support in the country if it wants to stay in power.)

Reciprocity may enable mobilization of internal support for concession y in country B as follows. Industry 1_A can mobilize industry 2_B in B to provide that support through promising a reciprocal action (support of concession x) in A.

To encourage the use of this internal mechanism of ‘pressure and support’ may require some minimum specification of concessions in respect to products traded. This was the case under the Dillon Round

negotiations, where exchanged concessions were linked to specific items in the tariff schedule. This also motivated the introduction of the exception list in the Kennedy Round which enabled a sector-by-sector and item-by-item approach. Otherwise the Kennedy Round relied on exchange of so-called linear or across-the-board concessions affecting principally all imports of the concession-granting country. Under that general formula the principal-supplier approach could not be practised without reference to the exception list and only reciprocity in a global sense might be reached.¹⁶

It seems that the draftsmen of the East-West reciprocity arrangements somehow neglected the existence of the 'pressure and support' mechanism. As will be shown below, the East European members of the GATT failed to use it, at least on the multilateral forum, to their advantage (see Chapters 6 and 7). Finally, some degree of 'pressure-and-support' mechanism is also present in the foreign-trade planning procedure in Eastern Europe. Although this has been understood by some of the big corporations engaging in East-West trade, it seems to be ignored by the Western policy-makers – at least when judged from the GATT experience (Chapter 4).

A reciprocity formula may be defined as expressing the character of concessions exchanged. In the GATT, it has been basically symmetric in nature. It relies on the exchange of concessions of an identical nature (tariff reduction, against tariff reduction). Given the shift of emphasis, however, from tariff protection to non-tariff barriers and the participation of target-protected economies in the GATT, the asymmetric formula of reciprocity may in the future become more frequent in multilateral trade negotiations. An asymmetric formula is one which provides for the exchange of concessions of a dissimilar nature. For example, a tariff reduction may be exchanged against some kind of quantitative import commitment as in the formula adopted for relations between Poland and the GATT. This type of formula, however, has an important disadvantage: it further complicates the process of negotiation by adding to the already difficult task of calculating the balance of costs and benefits the problem of equivalence between various instruments of concession-making (tariffs, quotas, import targets, licences, subsidies and so on).¹⁷ The more general the reciprocity formula, the more difficult it is to evaluate the potential effects of a policy chosen. Under a linear approach, effects of concessions are certainly less foreseeable and less understood than, say, under the item-by-item approach. The less specific and the more asymmetric the reciprocity formulas, the more difficult it is to evaluate the costs and benefits of concession-making. As will be seen later, this constitutes one of the obstacles of the East-West trade cooperation since the nature of trade control differs.

TARIFFS—MAIN PROTECTIVE ELEMENT

The multilateral trade order, as designed by the General Agreement, assumes a direct link between foreign and domestic prices. This being so, the GATT expects its members to control trade indirectly through prices rather than through direct instruments of trade control. Among the price instruments of trade control, the tariff occupies a key position. It facilitates identification of protectionist and discriminatory policies and is less discriminatory in nature than direct instruments of trade control. Accordingly, GATT provisions require that protection be afforded to domestic producers exclusively through the customs tariff.

No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party.¹⁸

The principle of the tariff as the main protective element manifests itself in several specific ways. Many GATT rules are either built around or are more easily practicable under the tariff. It is certainly true that MFN treatment and national treatment are more easily assessed under tariff protection. The GATT concept of regional integration also relies exclusively on tariffs as the instrument of protection. Use of the tariff instrument is thus an important aspect of participation in the GATT. The ceilings of nominal protection for members are principally expressed by the 'bound' rate of the tariff Schedules. During multilateral trade negotiations tariffs are also the main objects of bargaining. The GATT has already provided a framework for seven major tariff negotiations, the Tokyo Round being the most recent.

The central role of the customs tariff as an instrument of a country's participation in the GATT may raise some difficulties in applying the GATT provisions to the state-trading systems of Eastern Europe which rely on plan targets.

It will be shown that the tariff requirement is not necessarily incompatible with state-trading systems as such. Although it may be incompatible with those forms of state-trading that eliminate or limit the direct link between domestic and foreign prices. As noted above, that link constitutes a condition *sine qua non* of tariff-based trade control. Special attention will be paid to evaluating the roles tariffs play under specific types of state-trading.

ADAPTABILITY

One of the really important aspects of the GATT's role in international trade is the part it plays in shaping new developments in international trade relationships. Acting as a creator of rules, the contracting parties can adapt the GATT to new economic and political circumstances.

It is by means of the amendment procedure that the General Agreement may be most radically changed.¹⁹ Theoretically, it could have been used to accommodate the GATT to the needs of state-trading countries. If this was not done it was because the contracting parties preferred to establish their relations with Eastern Europe on a country-by-country basis.

Accession to the GATT is normally preceded by the negotiation of terms under which a newcomer will be admitted. This protocol for accession provides another suitable means of accommodating the GATT to specific circumstances.²⁰ (It served as the main method of accommodating the GATT to the needs of state-trading countries.) A newcomer can accede to the General Agreement with the accord of a two-thirds majority. A dissenting GATT member, however, has the right to require that any such accord should not be applied to its relations with the newcomer (Article XXXV). The United States invoked this article against Yugoslavia, Romania and Hungary in the initial period of these countries' membership.

The GATT also provides a waiver procedure (Article XXV:5) permitting release from specific rules of the GATT, when a country's economic circumstances so warrant. Finally, the GATT has incorporated some safeguard measures. For example, there are provisions on emergency protection which allow the postponement of tariff cuts or the imposition of quantitative restrictions on imports.²¹ Emergency action under the GATT must be non-discriminatory in principle, and a trading partner that suffers from a country's emergency protection may require some other concessions in order to offset its loss.

In general, the GATT is characterized by a considerable degree of flexibility as far as the establishment of obligations between members is concerned. This considerably facilitated the accession of East European countries to the General Agreement.

CONSULTATIONS AND INFORMATION

Secrecy and lack of information helps to render any machinery for trade cooperation non-operational. To eliminate that risk, therefore, GATT imposes certain requirements and makes additional recommendations concerning the dissemination of information.

Special reporting requirements exist under the GATT in relation to state trading, countervailing duties, subsidies, licensing, safeguard action

and other such activities. Consultations are another way of learning about the laws and trade practices of the GATT countries; the consultations on balance-of-payments restrictions are a good example.

The signatory countries of the GATT are encouraged to forward promptly to the GATT Secretariat copies of laws, regulations, and decisions, as enumerated in Article X. It is also recommended that they help the International Trade Center UNCTAD/GATT in identifying market opportunities, for example through the exchange of studies.

Consultations are the primary formal technique of policy coordination in the GATT. Invoked under several GATT provisions, they are especially intended to clarify difficulties relating to application of GATT rules. In addition, the GATT provides for periodic consultations on specific matters and *ad hoc* consultations. However, the formal structure of the GATT forum—the consultations and meetings of GATT members during the Sessions (or Council sittings) and working parties—is only the tip of the iceberg.

The GATT countries usually maintain permanent representatives in Geneva who have their fingers on the pulse of commercial relations as reflected in the GATT and other economic organizations. Since these representatives are in permanent contact with each other, there is a sort of informal forum within the formal structure of the GATT. The GATT Secretariat has a central position in that former structure. Although it is hard to evaluate the role of these informal consultations, they were certainly used for the negotiations leading to the accession of the East European countries to the GATT.

STATE TRADING

OCCASIONAL STATE TRADING

State trading is distinguishable from other types of trading by virtue of the link it implies between a trading enterprise and a state authority. Since the GATT was created for private enterprise economies, it was concerned only with the occasional form of state trading as practised in those economies.

As examples of state-trading enterprises in market economies the following units may be mentioned: the Tobacco Monopoly in France, the Food Agency in Japan and also the State-Trading Corporation in India. All these units differ considerably as to their objectives, organizational structure, financing and degree of dependence on the government. These differences constitute the main difficulty in handling the issue of state trading in an international trade organization.

The American 'Suggested Charter' (1946) defined 'state enterprise' as

an enterprise over which the government exercises 'directly or indirectly a substantial measure of control'.²² The draftsmen of the Havana Charter preferred to exclude this definition of 'state enterprise', considering it unsatisfactory.²³ Nor was any explicit definition of 'state enterprise' or 'state-enterprise' included in the General Agreement. The panel of experts convoked by the GATT, however, reached the conclusion that the term 'state-trading enterprise' referred either to:

an instrumentality of government which has power to buy or sell or to a non-governmental body with such power and to which the government has granted exclusive or special privileges.²⁴

For the purposes of this study one can name three types of state-trading links which, in the context of GATT practice, would constitute state trading:

(1) state ownership of the trading enterprise, even when it is a competitive one;

(2) direct control by state authorities over the trading operations of a private enterprise exceeding the permissible levels of control, for example, day-by-day management of trading by state authorities;²⁵ and,

(3) granting by the state of exclusive or special privileges to an enterprise which may result in imperfect competition on the market.

In its original version, the GATT was first concerned with the non-discriminatory operation of a state-trading enterprise. Except for some provisions on import monopoly, the GATT did not deal with the protectionist dimension of state-trading.²⁶

State-trading enterprises, like any other trading enterprises, are required under the GATT to act 'in a manner consistent with the general principles of non-discriminatory treatment'. To this end, three types of obligation concerning the state-trading enterprise and its government are outlined by the GATT. First, the General Agreement imposes on the government a negative obligation not to prevent any enterprise (state-trading enterprise included) from acting in a non-discriminatory manner and in conformity with commercial considerations. This puts some limits on government control of state trading.²⁷

Secondly, the GATT requires that the state-trading enterprise itself act in accordance with commercial considerations, which include 'price, quality, availability, marketability, transportation and other conditions of purchase or sale, and [the obligation to] afford the enterprises of the other contracting parties adequate opportunity, in accordance with customary business practice, to compete for participation in such purchases or sales'.²⁸

Thirdly, the GATT obliges the government to see that state-trading

enterprises import or export in a manner consistent with the principles of non-discrimination prescribed in the General Agreement in the government measures affecting private trade.²⁹

Other GATT rules directly affecting state-trading enterprises are concerned with monopoly.

Provisions on import monopoly of a product which is subject to tariff bindings require that the import mark-up be smaller than the tariff.³⁰

This may also be expressed as follows:

$$\left[\frac{p^d - p^f r}{p^f r} \leq t \right]$$

where

p^d = domestic selling price of the monopoly exclusive of internal taxes, transportation, distribution and other expenses incidental to purchase, sale or further processing and a reasonable margin of profit;

p^f = the landed cost in foreign currency;

r = exchange rate; and,

t = tariff rate fixed in relation to domestic price.

These provisions referring to tariff-bound import monopoly are to be applied in the light of a corresponding article of the Havana Charter, which provides for the obligation to: 'offer for sale quantities of the products as will be sufficient to satisfy the full domestic demand for the imported product.'³¹

The amendments to the General Agreement (1957) recognized that a state-trading enterprise 'might be operated so as to create serious obstacles to trade'.³² This might occur for two (implied) reasons:

(1) the state-trading enterprise might serve as 'a substitute for other measures covered by the General Agreement such as quantitative restrictions, tariffs and subsidies';³³

(2) special privileges granted to a trader by the state might result in a monopoly situation. A monopolistic trader in turn is likely to reduce trade below the free-trade level in order to maximize its profit. In other words, it may wish to increase the margin by which the price charged for the imported product on the domestic market exceeds the landed cost.³⁴

The GATT, though not concerned with restrictive business practices in respect to private traders, is concerned with the restrictive business practices of state-trading enterprises. The GATT recognizes that with occasional state trading, as practised in private enterprise economies, the monopoly and the trade-barrier aspects of state trading tend to be interrelated.³⁵

In order to deal with the protectionist dimension of state trading the GATT proceeds in two ways. First, it recognizes that the principles of negotiation recommended for tariffs may also be applied to protection obtained through state-trading enterprises. Negotiations are supposed to be directed towards:

the reduction of duties and other charges on imports and exports or towards the conclusion of any other mutually satisfactory arrangement consistent with the provisions of this Agreement.³⁶

Secondly, the GATT countries are requested to report those products exported or imported by state-trading enterprises. Inadequate reporting on the trading of such products required the establishment of a special questionnaire on state trading,³⁷ which is clearly conceived to account for occasional state trading as practised in market economies. Moreover, any GATT member maintaining import monopoly on a product not subject to tariff concessions or regulating exports or imports through the operations of a state-trading enterprise is obliged to supply relevant information on request by any other GATT country.³⁸

In conclusion, the GATT's state-trading provisions are clearly drafted to deal with occasional state trading in private enterprise economies. Nevertheless, some of these provisions are of general validity and may also apply to the state-trading systems. Others are based on the assumption of a direct link between domestic and foreign prices. Their validity is thus limited to those state-trading systems which rely essentially on the price instruments of trade control and free-price formation. The GATT rules for negotiations on state trading are broad enough to provide a basis for conclusion of special arrangements with a state-trading system if so desired.

STATE-TRADING SYSTEMS

On one occasion only does the General Agreement explicitly refer to a state-trading country ('a country which has a complete or substantially complete monopoly of its trade').³⁹

The GATT has tried to distinguish between state interference with trade through the state-trading link and state interference with trade through overt methods of trade control. This concept may be illustrated as shown in Figure 3.2.

Classification

Differences in the character of the state-trading link may serve as criteria for distinguishing between two types of state-trading systems.

In loose state trading the state either owns the enterprise or grants it exclusive privileges to support a monopolistic or semi-monopolistic

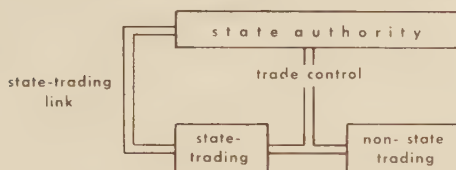


FIGURE 3.2
State-trading Link and Trade Control

position.⁴⁰ Once the state enterprise is established or the privilege granted, government interference is limited exclusively to trade control. This implies an open method of restricting or expanding trade through instruments acceptable to the GATT, such as tariffs, subsidies, quotas under defined circumstances and so forth. Under loose state-trading, there may be a degree of direct response between domestic and foreign prices and tariffs may be effective and primary instruments of trade control.

In command state-trading, freedom of the enterprise is limited by governmental orders. In the case of the centrally-planned economy, these orders are usually motivated by planners' objectives.

There may exist some important differences in the use of target control. Plan targets regulating foreign trade may differ in character and degree of product, and of country specification. Targets may be general, making no distinction between countries or areas, or they may be specific as to country or area. Targets may determine the volume of trade goods (volume targets) or their value (value targets); they may determine trade commodity-by-commodity (one-commodity targets) or they may refer to a whole range of commodities (multi-commodity targets).⁴¹

Models

If the analysis of the applicability of GATT provisions to the command state-trading systems is to be of any value some basic techniques of these systems have to be first clarified. Let us consider two simple models.

Model 1 (one-commodity targets). It is assumed that government interference with the operations of foreign trade units relies exclusively on one-commodity targets. These targets are not country-specific: it is thus up to foreign trade units to choose their import markets.

The foreign trade unit is subjected to the target-fulfilment criteria supplemented by the profit criteria. This means, in other words, that the income of the foreign trade managers is dependent both on the fulfilment of plan objectives and the capacity to choose the lowest-price offer.

Under these assumptions the foreign trade units will conduct their import activities as formulated in the following programme:

$$(I) \text{ Max } p^d \sum_{i=1}^m M_i - \sum_{i=1}^m p_i^f M_i r_i - E$$

Restrictions:

- (1) $\sum_{i=1}^m M_i = T$
- (2) $0 \leq M_i \leq \overline{M}_i$
- (3) $E = \text{constant}$

where

p_i^f = the landed cost of import from country i , $i = (1, 2, \dots, m)$ expressed in foreign currency;

p^d = domestic selling price of the foreign trade unit (exclusive of internal taxes, transportation, distribution and other expenses incidental to commercial transactions);

M_i = volume of imported product from country i , $i = (1, 2, \dots, m) \sim$ (The non-negativity restriction in reference to M_i means that no re-export is allowed);

T = one-commodity import plan target which determines the volume of imported product from the area of m countries (T is not discriminatory within that area because it is not country-specific);

r_i = commercial exchange rate for country i ;

E = tax evaluated *ex ante* for every T ;

$\overline{M}_i$ = maximum volume of a good that can be imported from country i (availability of a good at a given price).

The foreign trade unit aiming to fulfil the mandatory plan target T will import the required amount of a given good. In other words, it will respect the first restriction of the above linear programme

$$\left(\sum_{i=1}^m M_i = T \right).$$

The profit criterion leads the foreign trade unit to maximize the above linear profit function through choosing the closest foreign market with the lowest prices. In other words, under the one-commodity target the profit criterion is strong enough to induce the foreign trade units to act in accordance with commercial considerations as required by the GATT.

The role of profit criterion may, however, be limited by the introduction of a country-specific import target specifying that 'M_i' comes from a particular country or group of countries. Ideally, application of the GATT non-discrimination principle to such systems should require that no country-specific target controls be introduced.

Model II (multi-commodity targets). Profit criteria can play an even more significant role under multi-commodity plan targets. Here the profit criteria and target-fulfilment criteria induce the foreign trade unit to handle imports according to the following formula:

$$(II) \text{ Max } \sum_{j=1}^n \sum_{i=1}^m p_{ij}^d M_{ij} - \sum_{j=1}^n \sum_{i=1}^m p_{ij}^f M_{ij} r_i - E$$

Restrictions:

$$(1) \sum_{i=1}^m \sum_{j=1}^n p_{ij}^d M_{ij} = T$$

$$(2) 0 \leq M_{ij} \leq \overline{M}_{ij}$$

$$(3) E_j = \text{constant}$$

$$j = (1, \dots, n)$$

where

p_{ij}^f = the landed cost of import of good j from country i expressed in foreign currency, $i = (1, 2, \dots, m)$;

p_{ij}^d = domestic selling price of the foreign trade unit for product j ; the price is centrally adjusted or free;

M_{ij} = volume of imported product j from country i ;

$\overline{M}_{ij}$ = maximum volume of good j that can be imported from country i (availability of good at given prices);

T = n -commodity import plan target which determines the value of imported goods from the m -country area in terms of domestic currency;

r_i = commercial exchange rate for country i ;

E_j = tax evaluated *ex ante* for every n -commodity import target T .

In order to attain its (n -commodity) plan target, the foreign trade unit will compose its import basket, choosing from the range of $1, \dots, n$ goods, in such a way as to achieve the mandatory import value T . In other words, it will respect the first restriction of the above linear programme.

Profit motivation also has an important part to play. The foreign trade unit maximizes its linear profit function not only through choosing the best foreign market but also through determining the most advantageous product composition of imports (import basket) under a given n -commodity target T .

There may be, under this model, a limited direct link between domestic and foreign prices. As in Model I, choice of the best foreign market according to profit criteria can be limited under country-specific import targets. Consequently, as in the first case, attention should be paid to assuring the non-discriminatory character of import targets. These targets should be general rather than country-specific.

Trade Control

What role may be assumed by tariffs, subsidies, quotas, and other instruments of trade control in our two models of command state-trading?

In Model I, where the level of trade is determined by volume targets, instruments of trade control cannot effectively influence trade levels. In any case, by their very nature, tariffs, quotas and exchange rates are likely to implement discriminatory policies.

Another variant of Model I may be based on one-commodity value targets. If the import targets are specified in foreign currency terms, changes in the country's exchange rate will have no impact on its import level. However, tariffs may be effective if the customs payments are included in the purchasing cost of the foreign trade enterprise.

If the one-commodity value targets are expressed in terms of domestic currency (or a domestic accounting unit) and domestic prices are either free or centrally adjusted, both exchange rates and tariffs may become effective.⁴² But the preponderant instrument of trade control in command state-trading is the one-commodity plan target. Consequently, concessions referring to plan targets (import commitments), rather than to tariffs, should provide a basis for the system's participation in multilateral trade negotiations.

Tariff negotiations may acquire some practical importance in Model II. The multi-commodity targets may be supplemented by tariffs, quotas, subsidies and exchange rates. But here also the effectiveness of these instruments remains limited by the multi-commodity targets.⁴³ Let us elaborate this point.

Assuming that a foreign trade unit is guided by the target-fulfilment criteria supplemented by the profit criteria (see programme II on p. 49), its objective in imports may be summarized by the following linear programme:

$$(III) \quad \text{Max} \quad \sum_{j=1}^n p_j^d \cdot x_j \cdot r - \sum_{j=1}^n \sum_{i=1}^m [(1 + t_{ij}) P_{ij}^F] X_{ij}$$

Restrictions:

$$(1) \sum_{j=1}^n \sum_{i=1}^m p_{ij}^F X_{ij} = T_v$$

$$(2) X_{ij} \geq 0$$

where

p_{ij}^F = foreign price of commodity j in country i ;

t_{ij} = tariff rate for commodity j imported from country i ;

x_{ij} = quantity of commodity j imported from country i ;

T_v = n -commodity import target (value of imports indicated globally for n -commodities in terms of foreign currency);

p_j^d = domestic price of commodity j ;

x_j = quantity of imported commodity j ;

r = exchange rate.

In other words, the programme indicates that a foreign trade enterprise optimizes the commodity structure and country distribution of its imports under a given structure of domestic and foreign prices for n -commodities—given the country's tariff rate structure and a specific non-discriminatory multi-commodity import target (restriction(1) in the programme). It shows that, with multi-commodity targets, tariffs have some place as effective instruments of trade control. Broadly speaking, the greater the value of that target (T_v) and the wider the range of commodities it covers, the more likely the tariff may function as a supplementary instrument of trade control. Negotiations on tariffs could thus be considered a valid approach with this type of economy, providing, however, that they are accompanied by negotiations on the multi-commodity targets (import commitments). Moreover, under this system, attention should be paid to the non-discriminatory character of trade control measures and import targets.

TRADE CONTROL

DIRECT TRADE CONTROL

Direct trade control consists of restricting or expanding foreign trade by quantitative specification, using, for example, quotas or licensing. This method is often opposed to indirect trade control, which aims at restricting or expanding foreign trade through price mechanisms such as tariffs and subsidies.

During the preparatory work for the General Agreement, direct trade control was the object of important policy clashes among the proponents of three different attitudes. The United States considered that restriction of trade through direct instruments was the most extreme and worst form of protectionism and proposed an absolute ban on this type of trade control. They argued that direct control reinforced the tendency towards bilateralism and politicization of trade, introducing the dangers of discrimination and distorting the link between domestic and foreign prices.⁴⁴

The West European countries, recovering from the war, considered direct trade control an indispensable method of protection for balance-of-payments reasons. For India, and some other developing countries, direct control was an essential method of regulating trade in the interest of economic development programmes. The GATT approach to direct trade control was in a way a compromise of these three attitudes.

The GATT explicitly forbids the use of direct trade control. It allows, however, five important exceptions:

(a) quantitative restrictions are permitted to restore or maintain balance-of-payments equilibrium as provided by Article XII and in the case of the low-income economies by Article XVIII:B;

(b) the low-income economies are also allowed to use quotas to assist the establishment of particular industries (Article XVIII:C);

(c) quantitative restrictions have continually been used by the developed nations to protect agriculture (a very important exception);

(d) quotas are also permitted to prevent market disruption (Article XXI); and

(e) moreover, it is possible to use quantitative restrictions against 'scarce currency' countries (Article XIV).

The GATT recognized that its provisions on quantitative import or export restrictions 'include restrictions made effective through state-trading operations'.⁴⁵ Consequently, the provisions examined below are applicable to all forms of direct restrictions on trade in state-trading systems.

NON-DISCRIMINATION UNDER DIRECT TRADE CONTROL

Several means of assuring non-discrimination are possible under direct trade control. Non-discriminatory, direct allocation of trade may be accomplished on the basis of traders' previous shares, on the basis of the respective production capacities of exporting countries, or on a 'first come, first served' basis. For our purposes, the GATT requirements on non-discrimination under direct trade control may be divided into two

categories: requirements covering all quantitative restrictions, including restrictions made effective through the operation of state-trading enterprises; and requirements explicitly concerned only with quotas and licences without reference to the state-trading link.

Provisions on the non-discriminatory operation of quantitative restrictions falling into the first category require that the direct allocation of trade, when resorted to, must be applied to all GATT countries.⁴⁶ Trade allocation under direct trade control is required to approximate, as closely as possible, to the shares which the various GATT members might be expected to obtain in the absence of direct control.⁴⁷ When direct trade control is maintained for balance-of-payments reasons, the GATT permits the allocation of imports of different products, or classes of products in 'such a way as to give priority to the importation of those products which are more essential'.⁴⁸

These general provisions requiring non-discriminatory application of quantitative restrictions are specified only for quotas and licences. Here, the GATT approach may be summarized as follows.

The GATT is certainly more in favour of a global quota (a quota not allocated to specific countries or sellers) than of specific quotas. This is understandable since the global quota is a less discriminatory instrument of trade control. Under a global quota the direction of trade and the source of import can shift with changes in quality, cost and prices. The more specific the direct allocation – that is the more rigidly fixed the direction of export and source of import – the greater the danger of country discrimination.

When for some reason specific allocation is desired, therefore, the GATT proposes that the countries exporting the product seek an agreement on the allocation of shares in the quota.⁴⁹ Such agreements must take commercial considerations into account. If the application of these considerations by government authorities is then found to be impracticable, proportions derived from a previous representative period may furnish a point from which to evaluate 'changes in relative productive efficiency as between domestic and foreign products or as between different foreign products' and some other special factors.⁵⁰ The Havana Charter specified that these 'other special factors might also cover changes in the ability to export among various producers'.⁵¹

It is not clear, however, whether the same approach may be adopted under the GATT. Is a new producer allowed to establish the right to market under the 'representative period' approach? The answer is probably affirmative, considering the GATT's general requirements that direct trade allocation should approximate what could reasonably be expected in the absence of direct allocation. Also, in reference to determining what constitutes equitable shares of world trade where subsidizing is involved, the GATT working party agreed that one should

not lose sight of 'the desirability of facilitating the satisfaction of world requirements of the commodity concerned in the most effective and economic manner'.⁵²

The General Agreement also recognizes that export or import restrictions may be applied by means of licences.⁵³ The GATT requires that licences should not specify countries or source of import. They should be global rather than individual in character. Individual licences are permitted only for the purpose of handling specific quotas.⁵⁴

It is the duty of the GATT countries which maintain quotas and licences to provide information and allow consultation with regard to this form of control. In the case of fixed import quotas, governments are required to supply information on the quantity or value of quotas for the forthcoming period, as well as to make known all previous changes. The current shares in quotas, if fixed in advance, are to be made public and the respective information is to be sent to all interested GATT members. A similar obligation applies to a country that uses import licences. Such a country is required to supply information on the administration of the licensing system, past licences issued, and, if applicable, the country distribution of licences.⁵⁵

From this brief account of the rules of the GATT on direct trade control, several conclusions may be drawn. The GATT is concerned with two types of quantitative restriction – those traditional to private-enterprise economies (quotas and licences for example), and those 'made effective through state-trading operation' (both direct trade control over state trading and the state-trading link). The GATT tries to submit the quantitative restrictions implemented through state-trading links to the same general principle of non-discrimination affecting other QRs. The respective provisions, however, are too general to be effective, due to two omissions. While some explicit criteria of non-discrimination on quotas and licences are enumerated, no such criteria are formulated for the quantitative restrictions 'made effective through state-trading operation'. Whereas the information requirement is imposed for quotas and licences, no corresponding requirement is imposed on QRs made effective through state-trading operations. Moreover, a comparison between the GATT information requirements on state trading (which could be considered as a requirement to give information on QRs made effective through state-trading operations) and the information requirement referring to quotas and licences, differs in two important aspects. Whereas the latter calls for information on value or quantities of trade permitted for the forthcoming period, the former refers only to the past. Also any request for information on state trading may be considered contrary to commercial interests (Article XVII:4 (c)) and on these grounds not feasible, while no corresponding escape clause exists in the case of an information request referring to licences and quotas.

All in all, the GATT provisions on non-discriminatory direct trade

control may well be applied to the state-trading system. Yet, whereas they seem fully satisfactory for the loose state-trading system, more detailed rules are necessary if non-discrimination is to be meaningful for the command state-trading system.

TARIFFS

Tariffs, as noted above, are usually an essential instrument of government participation in the GATT and are supposed to be the main protective element. This requirement can certainly be fulfilled under the loose state-trading system. Assuming free domestic price formation (or centrally adjusted prices), and the existence of a direct link between domestic and foreign prices, governments maintaining loose state trading may adopt tariffs as a meaningful instrument of trade control in much the same way as essentially private-enterprise economies. A tariff-protected state-trading system can conform to GATT standards and undertake meaningful obligations regarding the ceiling of nominal tariff protection and non-discrimination. Consequently, negotiations with such a government on reciprocal reduction of protection can use the symmetric reciprocity formula which is practised traditionally by the tariff-protected economies of the General Agreement.

The GATT's tariff-based approach would be less valid as a basic arrangement for participation of command state-trading systems in the GATT. Under the multi-commodity variant, tariffs may only be used as a supplementary instrument of protection. Consequently, any meaningful reciprocity arrangement for trade between tariff-protected economies and a state-trading system maintaining multi-commodity targets would require an asymmetric reciprocity formula allowing the exchange of tariff concessions for concessions expressed in terms of plan targets. An asymmetric reciprocity formula is even more necessary when one-commodity targets determine the level of trade with the tariff-protected economies.

Since tariffs may be used as an instrument of discrimination in all categories of state-trading systems, the provisions of the GATT on non-discrimination under tariffs should be applied to state-trading systems.

EXCHANGE RATES AND EXCHANGE RESTRICTIONS

In regulating exchange rates, a government may differentiate among products, currencies or countries, and in this way introduce product, currency or country discrimination. The General Agreement relies on three ways of preventing its members from frustrating its objectives through exchange-rate action. It operates on the assumption that most of its members will seek cooperation with the International Monetary Fund. GATT countries which are not members of the IMF conclude

special exchange-rate agreements with commercial partners.⁵⁶ As a rule, however, these special exchange-rate agreements carry obligations similar to those imposed on IMF members. (Perhaps this is why the solution has proved unworkable.) The third solution consists of exempting a country (non-IMF member) from the obligation to enter into a special exchange agreement (Article XV:6) and subjecting it to other rules.⁵⁷ The provisions of these new rules, which are practically uniformly imposed on governments benefiting from a waiver from Article XV:6, are of two types.

Firstly, the countries concerned are obliged to act in exchange-rate matters in accordance with the intent of the GATT and in a manner fully consistent with the principles laid down in the special exchange-rate agreement. The obligation is reinforced by the fact that the exemption can be withdrawn if it is violated.

Secondly, the exchange-rate practice of the countries enjoying this special regime is subject to requirements regarding information and consultation. Formally, the obligation to inform means compulsory reporting on exchange-rate matters. In practice, however, this requirement is scarcely ever observed. This procedure can be used primarily in cases when a government is suspected of exchange-rate actions that have clearly abused the purpose of the GATT.

The approach of the GATT to exchange-rate action is fully acceptable to state-trading systems. Indeed, in the case of loose state-trading and command state-trading relying on value targets, exchange-rate action may influence the level of trade and cause discrimination. In the case of command state-trading based on volume targets it may only cause discrimination.

SUBSIDIES

The General Agreement is generally against both production subsidies and export subsidies. Although it does not forbid subsidies, as such, it subjects their use (especially export subsidies) to certain limits and requirements. Three types of obligations connected with use of subsidies can be distinguished.

GATT members are required to give notification on any subsidy which influences the level of trade, directly (export subsidy) or indirectly (production subsidy), and to consult on subsidies when so requested.⁵⁸

A second obligation forbids export subsidies on primary products which would bring the subsidized exporters 'more than an equitable share of world export trade'.⁵⁹ This requirement, introduced in 1955, is currently accepted by all GATT countries, and newly acceding states are usually bound by it.

A third obligation – to cease export subsidies on any non-primary products – applies to a small group of developed countries, and no

newly acceding states (under Article XXXIII) are bound by it unless they sign the relevant declaration.⁶⁰

Although the GATT does not prohibit subsidies, members are permitted to use countervailing duties against subsidized products.⁶¹

As far as the state-trading systems are concerned, it is important to note that subsidy is understood by the GATT to be an effective instrument of trade control—a means of increasing exports. In the interpretation of the experts brought together by the GATT: ‘the phrase “increased export” . . . was intended to include the concept of maintaining exports at a level higher than would otherwise exist in the absence of the subsidy’; and ‘the criterion is therefore what would happen in the absence of a subsidy’.⁶²

This interpretation may considerably limit the applicability of the GATT provisions on subsidies (and countervailing duties) to the target-protected economies. But it can be argued that under one-commodity targets the level of exports is determined directly and the eventual negative tax paid to the foreign trade unit is the result of, and not the reason for, a given export performance.

The rules of the GATT on subsidies may become clear when applied to a system protected through multi-commodity plan targets. Here too, however, certain difficulties exist. Although, under multi-commodity targets, subsidies could be used to influence the level of trade within the target framework, the operation of plan targets may require an equalization system. In practice it may be very difficult, if not impossible, to distinguish between equalization payment (which is an implicit subsidy under a plan target but not in the GATT sense) and the explicit subsidy, one that influences the level of trade within the target framework. When discussing ways of determining the existence or non-existence of a subsidy, the GATT panel recommended that in all ‘doubtful cases’ countries should supply information on the matter. The contracting parties, then, would have to determine whether or not the particular instance might be considered subsidizing.⁶³

DOMESTIC PRICE FORMATION

Domestic price control may result in an increase in protection above the level agreed upon by the GATT countries in tariff schedules. Tariff concessions, therefore, require a guarantee that domestic price controls will not make these concessions illusory.

The General Agreement calls for those of its members who apply internal price controls to take into account ‘the interest of exporting contracting parties with a view to avoiding to the fullest practicable extent any prejudicial effects’.⁶⁴

Certainly the GATT measures on domestic price formation have a practical meaning for loose state-trading systems which maintain direct

links between domestic and foreign prices. They are however, practically meaningless to command state-trading systems where there is either no link or a very limited link between domestic and foreign prices.

The question of domestic price formation is closely related to the problem of dumping.⁶⁵ The GATT provisions on dumping may be fully applicable to a country maintaining a loose state-trading system and price formation that conforms with GATT standards. But this is not necessarily the case for command state trading. The GATT recognizes that it is not always appropriate to make a strict comparison between centrally-fixed domestic prices and export prices in a country maintaining a complete monopoly over its trade.⁶⁶ Participation in the GATT of the command state-trading systems might thus require more precise criteria for dealing with dumping and countervailing duties.

DISCRIMINATORY TRADE ARRANGEMENTS

BILATERAL TRADE ARRANGEMENTS

Multilateralism—the balancing of a country's exports and imports globally and not *vis-à-vis* individual trading partners—is one of the main policy aims of the GATT-IMF system. Since foreign trade conducted on the basis of bilateral trade agreements could involve discriminatory trade policies, the question of the compatibility of these arrangements with the rules of the GATT is an important issue. It can be examined in respect to the four categories of bilateral trade agreements.

The first category includes agreements which contain a so-called exchange equilibrium clause, meant to balance export receipts and import expenditures on a bilateral basis. This type of agreement is basically forbidden under the GATT-IMF system. Article XI Section 2 of the IMF Agreement reads:

'Nothing in this Agreement shall affect the right of any member to impose restrictions on exchange transactions with non-members or with persons in their territories, unless the Fund finds that such restrictions prejudice the interests of members and are contrary to the purpose of the Fund.'

The Fund concluded that imposing restrictions on exchange transactions with member countries of the GATT, even if non-members of the IMF, would be contrary to the objectives of the Fund.⁶⁷ Thus the obligation of IMF members not to impose restrictions on exchange-rate transactions with each other is extended to include non-IMF members of the GATT. Any exception to this general rule requires explicit permission from the Fund.

The second category of bilateral trade agreement covers arrangements providing for import commitments or quota allocations. The GATT condemns import commitments and quota allocations, mainly because they tend to lead to discrimination. When special circumstances require this type of bilateral trade agreement, its compatibility with the GATT may be examined in the context of the provisions referring to the administration of quantitative restrictions. As noted above, the applicability of these provisions towards command state trading presents difficulties.

The third type of arrangement encompasses bilateral agreements providing for preferential tariff treatment. These agreements have to be examined in the context of GATT requirements on MFN treatment and in the light of GATT provisions on regional integration (Article XXIV). When the nature of the preference does not fall under regional integration in the sense of Article XXIV, the preference may be maintained only on the basis of a waiver.

The fourth category of bilateral trade agreements includes arrangements which do not provide for preferences but rather establish a specific code of commercial conduct compatible with the GATT – for example, arrangements on commercial arbitration specifications of dumping criteria and so forth. This type of agreement may provide a useful supplement to the General Agreement and may contribute to the improvement of direct contacts between traders.

Neither state trading nor central planning in foreign trade implies bilateralism *per se*. If bilateralism has resulted from certain planning techniques, these should be changed for other planning techniques, which does not mean that planning, as such, should be abandoned.⁶⁸ In other words, the two types of state-trading systems analyzed above could conform to the GATT requirement of multilateralism assuming that certain conditions were respected: no bilateral trade preferences and no country-specific import and export targets that result in bilateralism.

REGIONAL INTEGRATION

Regional integration is often just another term for discrimination. It opens some doors and closes others. For that reason the introduction of provisions permitting regional integration, as an exception to MFN treatment, entails the marking of strict limits as to the mode of freeing trade within a narrow geographical area.

Article XXIV of the GATT recognizes 'the desirability of increased freedom of trade by the development, through voluntary agreements, of closer integration between the economies of the countries parties to such agreements'. But at the same time the GATT defines the method of regional integration allowed.

Generally speaking, two economies are integrated when they are subject, without artificial distinction to one market or one planner, or both.⁶⁹ According to the General Agreement, which is concerned only with current trade transactions, two economies could be considered integrated when their trade and corresponding payments were subject to perfect competition or perfect computation or both (planner sets only free trade plan targets).

The method of regional integration, though, as permitted by the GATT, relies exclusively on the market mechanism. Article XXIV enumerates two forms of regional integration: customs union and free trade area. Neither of the two includes a central direct allocation for intra-area trade or restrictive plan targets as methods of protection through the state-trading link.

The approach may be fully applicable to a loose state-trading system which maintains tariffs as the main instruments of protection. There is no place under GATT provisions for regional integration of the command state-trading systems. Neither do these provisions deal with the regional integration of a command state-trading system with a market economy.

SUMMARY AND CONCLUSIONS

Fundamentally the GATT is based on a market-economy view of world trade, where state authorities which collect duties, fix standards and so on, are clearly distinct from the traders themselves. The GATT recognizes state trading as a permissible form of trading, although it was originally concerned only with occasional state trading as practised in the essentially private-enterprise system.

The GATT approach to state trading is certainly acceptable for the loose state-trading system, where the character of the state-trading link is limited either to state ownership of a trading enterprise or the granting of privileges which may give the trader a monopolistic position on the domestic market.

Difficulties in the application of the rules of the GATT could arise in the case of command state-trading systems. For, here, it is possible to implement protectionist and discriminatory policies through the state-trading link (plan targets), without recourse to the trade-control instruments which are subject to GATT regulations. If the command state-trading systems are to be admitted to the GATT, new rules would have to be added to the GATT code of conduct.

It might be desirable to incorporate into the GATT precise requirements on the non-discriminatory character of the state-trading link. In addition, an agreement on a new reciprocity formula would be needed if negotiation of concessions between the tariff-protected and target-

protected economies were to take place. GATT provisions on subsidies and countervailing duties would have to be modified and a more precise statement of GATT rules on dumping formulated if the traditional safeguard mechanism of the GATT are to work for relations with the command state-trading systems. Finally, provisions of the GATT on regional integration may need to be modified in order to submit the command state-trading systems to requirements similar to those of the tariff-protected economies.

NOTES AND REFERENCES

1. See GATT, Article XXIV. Moreover, the so-called 'grandfather clause' explicitly permits certain specified preferential arrangements under which the most important were the British Commonwealth preferences. See GATT, Article I:2.
2. Provided that the action is relevant to military supplies or fissionable materials, or is taken at a time of emergency in international relations.
3. GATT, Article II:1.
4. A passing reference to 'reciprocity' in the text of the General Agreement may be found in the Preamble and Article XXVIII *bis* (Tariff Negotiations).
5. It is not necessary, as sometimes assumed, that A suffer a loss when granting concession x to B. It is sufficient that concession x be of some value to B so that B is willing to pay for concession x by granting reciprocal concession y to A. However, this does not exclude that A's desire for reciprocity may be reinforced by a loss while granting concession x. In such a case, A has an additional reason for demanding reciprocal concession y from B.
6. The effects of granting the concession will not only depend on new trade flows but on the existing ones as well.
7. This argument is elaborated upon by Harry G. Johnson, 'An Economic Theory of Protectionism: Tariff, Bargaining and the Formation of Customs Unions', *The Journal of Political Economy*, Chicago, June 1965, pp. 264-7.
8. See, Józef Wilczynski, *The Economics and Politics of East-West Trade* (New York: Praeger, 1969) p. 95.
9. Robert Mundell's concept is briefly referred to by Johnson in 'An Economic Theory of Protectionism'. *The Journal of Political Economy*, June 1965, p. 258.
10. As a counter-argument, it may be claimed that East European industrialization highly depends on purchases of Western industrial equipment, the import of which cannot be interpreted as a 'cost' in terms of preference for industrialization. In that sense it could be considered that the East European claim should refer only to import concessions on industrial consumer goods. Moreover, if industrialization is an objective of the East European economic policy, it will be stimulated by Western market openings on industrial rather than agricultural products.
11. Gerard and Victoria Curzon rightly noted that all negotiators return home with their own calculations, proving that they have succeeded in negotiating an advantageous trade bargain, meaning that the export opportunities are greater than the import openings conceded. This logically cannot be true for all of them.

See Gerard and Victoria Curzon, *op. cit.*, pp. 160–1.

12. Ernest H. Preeg, *Traders and Diplomats* (Washington: Brookings Institution 1970) p. 23. Jagdish Bhagwati reaches a similar conclusion in respect of developing countries. See Bhagwati, 'Trade Liberalization among LDC's Trade Theory, and GATT Rules', in J. N. Wolfe (ed.), *Value, Capital and Growth* (Edinburgh: Edinburgh University Press, 1968) p. 32.

13. See Chapter 6.

14. See, for example, the Austrian complaint made against Poland at the forum of periodic consultations. GATT *Basic Instruments*, 13th Supplement, 1965, p. 34.

15. Plan target involves an order from the planner to the foreign trade units to import or export a defined amount of products. For a more extensive discussion of target-protected economies and the role that exchange rates may assume under a particular system of central planning, see below.

16. By a principal supplier in tariff negotiations is usually meant a country whose share in exports of a given product exceeds 10 per cent, or who is among the three to four main exporters of the good subjected to negotiations.

17. The usual difficulties in evaluation of costs and benefits resulting from particular concessions are due to complexity of the methodological approach and the lack of necessary statistical data. Removal of barriers to trade is likely to result in lower prices in the importing country. However, the additional amount of imports depends on numerous unmeasurable factors: price elasticity of demand in the domestic market, foreign elasticity of supply, degree of complementary and substitution in consumption, terms-of-trade effects, volume of new trade generated, and so on.

18. GATT, Article XI:1.

19. GATT, Article XXX.

20. The author learned a great deal about the legal aspects of the GATT from a very ambitious study by John H. Jackson, *World Trade and the Law of GATT* (Indianapolis, Kansas City, New York: Bobbs-Merrill, 1969) pp. xi–948. This extensive analysis of the General Agreement provides an excellent guide for anyone dealing with matters of world trade law. The reader can find there a detailed analysis of the amendment procedure, accession procedure and practically all other legal aspects related to the functioning of the General Agreement which are referred to in this chapter.

21. GATT, Articles VI, XI:2 (c), XII, XVIII:2, XIX, XX, XXV, XXVIII.

22. 'Suggested Charter', Article XXVI:2.

23. *Preparatory Committee of the United Nations Conference on Trade and Employment*, E/PC/T 160 (Geneva: United Nations, August 1947) p. 4.

24. GATT *Basic Instruments*, 9th Supplement, 1961, pp. 183–4.

25. It is difficult to draw the line between permissible control by state authorities (in the GATT sense) and the non-permissible control which would make that enterprise a 'state-trading' one. The GATT's panel of experts considered, for example, that 'the exercising of overt licensing power' over an enterprise is not sufficient to consider the trading of that enterprise as 'state trading'. GATT *Basic Instruments*, 9th Supplement, 1961, pp. 183–4.

26. The level of protection provided through operation of a state-trading enterprise could be limited by Article II:4. However, provisions of this Article refer only to products on which tariff concessions had been granted.

27. GATT, Article XVII:1.
28. GATT, Article XVII:1(b).
29. GATT, Article XVII:1 (a).
30. GATT, Article II:4.
31. Havana Charter, Article XXXI:5. For interpretation see Kenneth W. Dam, *The GATT, Law and International Economic Organization* (Chicago and London: The University of Chicago Press, 1970) pp. 325–6.
32. See GATT, Article XVII:3.
33. GATT *Basic Instruments*, 9th Supplement, 1961, p. 183.
34. This idea underlies provisions of Article XVII: 4 (b) of the GATT.
35. This view was widely accepted by draftsmen of the General Agreement. See *Verbatim Report*, E/PC/T/A/PV/22 (Geneva: GATT Secretariat, July 1947) p. 7.
36. See GATT, Interpretative note to Article XVII:3.
37. 'New questionnaire on state-trading', GATT *Basic Instruments*, 9th Supplement, 1961, pp. 184–5.
38. GATT, Article XVII:4 (c).
39. GATT, Interpretative note to Article VI.
40. Some draftsmen of the General Agreement argued that there was no reason for a state to maintain state-trading enterprises when no particularly extensive measures of control could be applied towards them. However, it should be noted that the concept of state trading understood exclusively as a form of enterprise ownership is fully understandable in the context of the socialist market economy. An original, clear-cut framework for analysis of state trading, though not fully acceptable in the context of the GATT practice, has been provided by Harriet Matejka, 'State-Trading: Instrument or Object of Trade Control?', *Journal of World Trade Law*, Twickenham, March–April 1974, pp. 209–14.
41. The above target classification follows the approach of Harriet Matejka, *Trade Control in Eastern Europe* (London: Macmillan, for the Trade Policy Research Centre, forthcoming).
42. Centrally adjusted price system means central price computation mainly according to changing conditions of supply and demand in the domestic economy.
43. The multi-commodity value target is defined in terms of foreign currency.
44. *Verbatim Report*, E/PC/T/A/PV/22 (Geneva: GATT Secretariat, July 1947) p. 13.
45. Interpretative note to Article XI, XII, XIII, XIV, and XVIII.
46. GATT, Article XIII:1.
47. GATT, Article XIII:2.
48. GATT, Article XII:3 (b).
49. GATT, Article XII:2 (d).
50. GATT, Article XIII:2 (d) and interpretative note to that article, as well as, interpretative note to Article XI:2 and XIII:4.
51. Havana Charter, Interpretative note to Article XXII:2 (d) and XXII:4.
52. GATT *Basic Instruments*, 3rd Supplement, 1956, p. 226.
53. GATT, Article XIII:2 (b).
54. GATT, Article XIII:2 (c).
55. GATT, Article XIII:3 (a) and XIII: 3 (c).
56. In their Resolution of 20 June 1949 the Contracting Parties adopted the model text of the special exchange agreement.

57. A waiver from Article XV:6 was granted, for example to Czechoslovakia. However, several developed market economies also benefited from the exception.
58. GATT, Article XVI:1. For legal discussion on subsidies see John H. Jackson, *op. cit.*, p. 376.
59. GATT, Article XVI:3.
60. GATT, Article XVI:4.
61. GATT, Article VI.
62. GATT *Basic Instruments, 9th Supplement* 1961, p. 191.
63. However, it is up to each member country of the GATT to determine whether the application of countervailing duties is justified. *Ibid.*, p. 191.
64. GATT, Article III:9.
65. GATT, Article VI includes provisions on dumping. For their analysis see John H. Jackson, *op. cit.*, pp. 411–24.
66. See GATT, interpretative note to Article VI.
67. Joseph Gold, *The Fund and Non-Member States. Some Legal Effects* (Washington: IMF, 1966) p. 28.
68. Bilateralism in East European trade is due to the lack of convertability rather than to the fact that these economies are centrally planned. See Franklyn Holzman, 'Soviet Central Planning and its Impact on Foreign Trade Behavior and Adjustment Mechanism', in Alan Brown and Egon Neuberger (eds), *International Trade and Central Planning* (Berkeley and Los Angeles: University of California Press, 1968) p. 286.
69. Peter Wiles, *Communist International Economics* (Oxford: Oxford University Press, 1968) pp. 306–7.

State Trading in Hungary, Poland and Romania

The following analysis, which is closely related to the findings of the preceding chapter, deals with the three East European foreign trade regimes at the moment of their accession to the GATT. It determines to what extent a state-trading unit in itself constitutes a barrier to trade; and how protectionist and, eventually, discriminatory policies are implemented both through the state-trading link and trade-control measures. Finally, it analyzes the bilateral trade arrangements and deals with problems posed by the CMEA in the GATT.

STATE TRADING

STATE MONOPOLY OF FOREIGN TRADE

In Hungary, Poland and Romania, political and social systems are based on state ownership of the means of production. Because imports and exports are almost the exclusive domain of state-owned enterprises, these countries have been referred to as 'state-trading countries'. A government's claim to the exclusive right of conducting foreign trade is often referred to as a state monopoly of foreign trade.¹ The institutional organization of a state monopoly of foreign trade can take various forms. Communist authorities, for political and economic reasons, have often chosen to adopt a highly centralized institutional type of state monopoly. Such was the case of Soviet Russia which in 1918 established a highly centralized framework of foreign trade institutions and regulations. The same was true of the so-called 'Stalinist model' of state monopoly which developed in the Soviet Union in the 1930s and was accepted in the post-war period by the other countries of Eastern Europe.

Hungary, Poland and Romania, while acceding to the GATT, maintained a monopoly of those institutions which were responsible for drafting and executing the foreign trade plan. This monopoly consisted

of a hierarchy of organizations including the State Planning Commission, the Ministry of Foreign Trade, insurance and transport organizations, the Chamber of Commerce, and enterprises authorized to carry out import and export transactions. The 'valuta' monopoly was run by the Ministry of Finance, the State Bank, the Foreign Trade Bank and the central customs administration.² The monopoly drafted a uniform plan for the foreign trade sector and conducted foreign trade transactions. It assigned individual economic units to specific sectors of foreign trade activities and defined their product competence as well as rights and obligations in foreign trade. It defined trade and exchange policy measures in line with central objectives and evaluated the effectiveness of these measures.

The state-owned enterprises that conducted foreign trade transactions were operational units of the trade monopoly. These units were separated from the state in the legal and financial sense. They were not liable for any obligations contracted by the state and *vice versa*. They owned and disposed of property and had the right to assume contractual obligations within the operational responsibilities defined by the Ministry of Foreign Trade. The state intervened in the operation of these units through channels which have been previously defined as state-trading links and through those instruments of trade control recognized by the GATT.

In Hungary, Poland and Romania, the basic operational state-trading links were foreign-trade plan targets. For that reason, findings related to the state-trading models, which are outlined in Chapter 3 above, are of some use when dealing with the three East European trade regimes.

In Hungary plan targets regulated trade with the CMEA countries and certain other centrally-planned economies. They applied to above 60 per cent of Hungary's trade. For the most part, however, Hungarian trade with the market economies was conducted outside plan targets and was regulated through tariffs and export subsidies, supplemented by quotas and licences. In Poland and Romania, on the other hand, all foreign trade was, in principle, subject to target control.

Multi-commodity targets were primarily used in these three countries. Targets tended to be more commodity-specific for trade with the centrally-planned economies than with the market economies and for imports rather than for exports.³ Multi-commodity targets in machinery, industrial plant and equipment fixed only very approximate limits for groups of commodities. Multi-commodity targets for consumer goods were also mostly general. In Poland, for example, the multi-commodity target for consumer imports – called 'sundry products' – covered about 15 per cent of total imports. It included products of particular importance to small and medium-sized Western exporters, such as foodstuffs, textiles, tobacco products, cosmetics, and so on. One-

commodity targets regulated trade for a limited number of products listed in the National Plan. These were usually goods of primary significance for the economy, mostly raw materials and agricultural products such as iron ore, steel, petroleum, grain and cotton, to use Poland as an example.

In Poland and Romania targets differentiated between payments through clearing and payments in hard currency. Targets for the clearing area were usually country-specific, whereas targets for the hard-currency area were global. In that sense targets for the clearing area were more discriminatory than targets for the hard-currency area. The implicit tax rate, however, seemed, on average, higher for trade with the convertible-currency area than for trade with the clearing area. So, from this viewpoint, targets for the hard-currency area were the more discriminatory.⁴ In Hungary, Poland and Romania targets were drawn first for production and exports, then for imports. The export-first approach reflected the relative importance that planners attached to the comparative scarcities of goods on the foreign market and at home.

In all three countries the foreign trade targets were set by bargaining among individual industries, producers and the central administration. This fact is of importance in the light of our discussion on reciprocity in commercial policy bargains among GATT countries (see Chapter 3). There it was noted that internal mechanisms of 'pressure and support' in the market economies provided an important argument for reciprocity in tariff negotiations.

Could it be maintained that there is a similar mechanism at work in the centrally-planned economies within their foreign trade planning process? Decision-making in the East European planning of foreign trade is briefly illustrated in Figure 4.1.

The foreign trade planner, first, submits indicative plans and prospects to particular economic units. These are considered by the economic units and preliminary requirements for production, or foreign trade schedules, are drawn up and passed back to the planner. The final decision should ideally fall within the competence of the planner. It is supposed to reflect central preferences, assure balance of payments, bilateral balancing of clearing areas, and so forth. In the absence of objective foreign trade criteria, however, the import targets are to a great extent the result of bargaining between the central authorities, the branch administration, and producers and traders. It is thus possible for Western exporters to mobilize internal support for advantageous market openings in Eastern Europe through reciprocal support of East European demands for market openings in the West.

The fact that this possibility has not been exploited much by Western exporters (especially small and middle-sized firms) stems, in part, from their lack of knowledge concerning the East European environment and

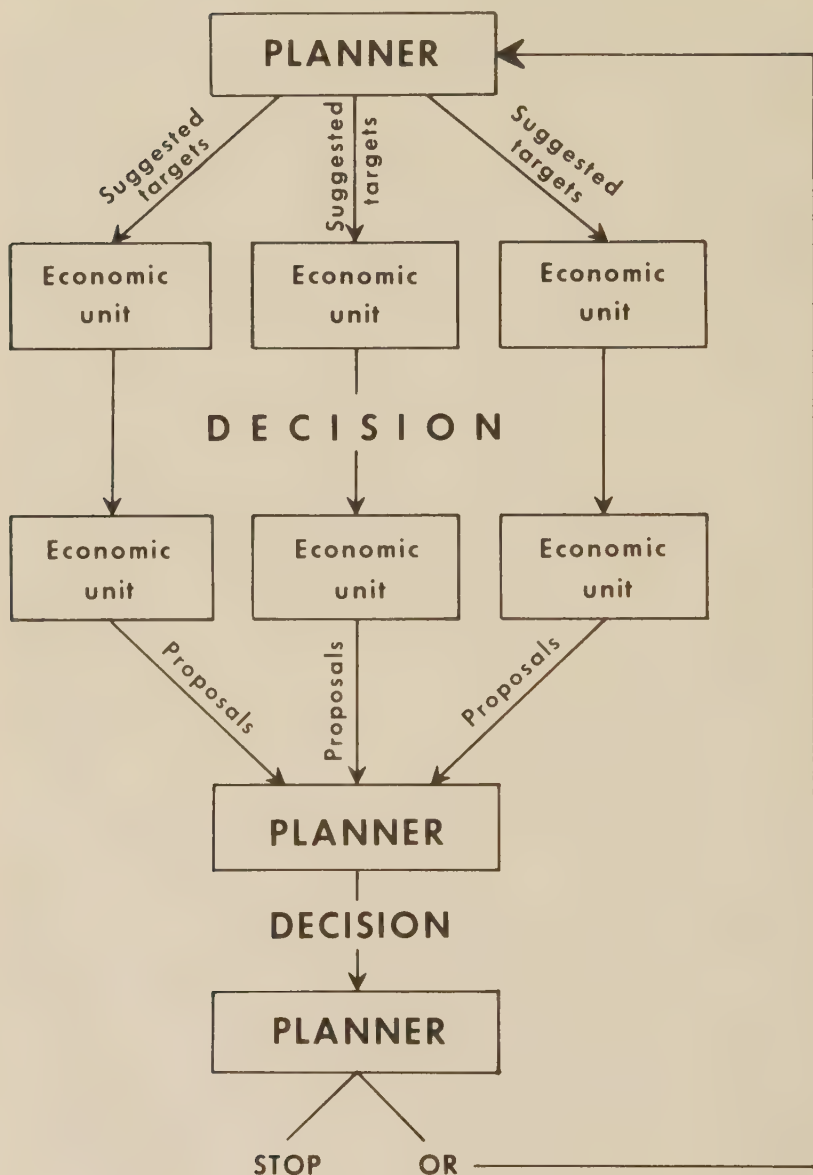


FIGURE 4.1
Planning of Foreign Trade

also the relative isolation of East European management and marketing systems from the West.

It can be briefly concluded that the foreign trade regimes of Hungary, Poland and Romania are state-trading systems in the sense previously defined. While Hungary's regime for trade with the West may be considered an example of loose state-trading, the foreign trade systems used by Poland, Romania and Hungary for trade with the centrally-planned economies come closer to the command state-trading model. As a rule, in Poland and Romania, targets were not country-specific; consequently they could not implement discriminatory policies towards particular countries. They distinguished, however, between convertible and non-convertible currency areas.

COMMERCIAL CRITERIA

When Hungary, Poland and Romania acceded to the GATT, profit criteria influenced the operation of state-trading enterprises in all three countries. In Hungary this was the main force motivating the Hungarian foreign trade unit operating in market economies.⁵ In Poland and Romania, profit criteria supplemented the target fulfilment criteria.⁶ But even here it was important enough to induce trade units to act in accordance with commercial considerations as required by the GATT.

In both countries export receipts and import expenditures were taken into consideration when judging the success of trade units and determining the revenue of their employees. In Poland, under the system of 1966, foreign receipts were converted at the appropriate exchange rate. Export costs were estimated in terms of the average factory price or internal transaction price and were adjusted for two factors: the disparity between the internal and external prices of materials and a uniform sales tax. The differences between export earnings and export costs, computed in this way, indicated the profit which served as the basis for premium calculation.⁷ In 1971 this system was abandoned, and, as in Romania, foreign trade receipts and expenditures were integrated directly into producers' accounts at prices reflecting foreign value.

The profit criterion was thus an important incentive for the East European managers conducting foreign trade operations and the foreign trade units in the three countries, therefore, were concerned with prices, quality of goods, availability, marketability and other conditions of purchase and sale (compare the models in Chapter 3). They sought all possible tenders. Inquiries were sent to potential suppliers inviting them to submit offers.

In Poland, Romania and Hungary the domestic producers could influence the choice of foreign partners. It is thus of interest to note how the domestic producer's criteria could differ from those of the foreign

trade unit. In Poland, for example, the method of calculating export profits adopted by the industrial branch administration and the producers omitted the cost of transportation and insurance in foreign trade transactions: export revenue was accounted on a free-on-board price (f.o.b) basis. Consequently, foreign trade units could be pressured by producers to depart from commercial criteria. Moreover, additional disparities between producer and trade unit criteria for profit maximization may have resulted from the differences in the efficiency formula used by traders and producers in particular production branches.⁸

The above analysis is based on the assumption that, aside from trade control instruments, state interference in foreign trade operations was implemented through plan targets (Poland and Romania) or was absent from trade with the West (Hungary). In general this assumption seems to be justified in the light of foreign trade practices in Hungary, Poland and Romania. Nevertheless, two reservations should be pointed out: the procedure for nominating the manager of the trade unit and the competence of the state authorities to judge the results of a unit's operation.

Along with the right to nominate the managerial staff, ministry officials could assert their authority and give operational instructions to the foreign trade managers. In this way they could induce a trade unit to deviate from the application of commercial considerations.⁹ The Ministry's authority to judge the economic results of trade operations also increased the dependence of trade managers on informal instructions. The importance of the above factors should not, however, be exaggerated, since they can be identified in many non-state-trading countries belonging to the GATT.

It can thus be contended that the Hungarian, Polish and Romanian trade units tend to be naturally influenced by commercial considerations. Assuming then that they are not subject to discriminatory targets, they are quite able to fulfil the respective requirements of the GATT.

NON-COMPETITIVE ENTERPRISE

The state monopoly over foreign trade in Hungary, Poland and Romania involved the limited participation of state-owned traders and producers in foreign trade activities. A major part of foreign trade in the three countries was carried out by foreign trade enterprises established for the sole purpose of conducting export and import transactions for a defined range of products. At the moment of accession to the GATT, foreign trade units operating in Poland, Romania and Hungary totalled forty-two, fifty-six and seventy-two respectively.¹⁰

They were generally state-owned, occasionally cooperative, and were subordinate either exclusively to the Ministry of Foreign Trade, or to the

latter as well as to the ministries of other economic sectors. When they acceded to the GATT, the foreign trade of the three countries was conducted by enterprises reporting exclusively to the Foreign Trade Ministry, although this later changed in Poland and Romania.¹¹ The scope of activities of foreign trade enterprises was strictly defined by the Ministry of Foreign Trade. The enterprises were empowered to conclude trade deals with foreign exporters and importers only within the limits laid down in their statutes. As a general rule, the trade enterprises specialized in a narrow range of industrial equipment and raw materials and in a broader range of consumer goods.

The majority of domestic producers and end-users were obliged to seek the services of the trade enterprises in order to sell their products on foreign markets or to import.

The normal formula – used in about 70 per cent of contracts – was based on a commission. Other contracts were based on partnership or sales for an enterprise's account.¹² Generally the Hungarian trade enterprise would conclude an annual contract with its consigner (industrial enterprise or domestic trader). Actual import and export deals were conducted on the basis of general contracts: each purchasing order was issued separately. The buying order specified the goods, quality, packing instructions, the consignor's 'limit price', preferred payment terms and delivery date. During negotiations of the import transaction with foreign suppliers, the trade enterprise was bound to observe all prescriptions in the consignor's buying order and was materially responsible for complying with these instructions. In Poland and Romania, although to a lesser degree, domestic manufacturers and groups of manufacturers also concluded commission contracts with trade enterprises. An important volume of trade, however, was conducted by the trade enterprises for their own accounts.

In addition to the traditional state-owned units in Eastern Europe there were several trade enterprises of a special character. In Hungary, for example, three share companies established by Hungarian producing enterprises functioned as independent foreign trade organizations.¹³ There were also several foreign-trade enterprises operating in conjunction with agencies of foreign firms; these were corporations or limited liability companies.¹⁴ In Romania and Poland several commercial companies were free to import and export any type of goods, usually for hard currency or through barter arrangements.¹⁵ Alongside those trade enterprises in all three countries, an ever-increasing number of big economic units (producers and commercial enterprises) carried out independent foreign trade activities in products with which they were directly concerned. In Poland, and to a greater extent in Hungary, trading rights had already been granted to certain producing enterprises and domestic traders. At the time of its accession to the GATT, Romania also granted authority to industrial associations to export and

import directly, especially those products that required technical knowledge.¹⁶ At the moment of accession to the GATT, Hungary maintained some sixty-five such enterprises, Poland five and Romania forty-five. Romania announced the granting of foreign trade rights to certain producing and trading enterprises, as well as the extension of the role of associations in the foreign trade sector.

From the preceding outline of the organizational structure of foreign trade monopolies, it is clear that there was a likelihood that some economic units would exert monopoly and monopsony power on the domestic markets. This could be attributed mainly to:

- (a) the limitation of enterprises allowed to participate in the foreign trade sector (Hungary: 140 units, Poland: 70 units, Romania: 88 units);
- (b) the strictly-defined non-competitive division by product of the foreign trade units; and,
- (c) the existence of a number of large industrial enterprises.

Due essentially to central price formation, lack of tariffs as the main protective element, and maintenance of plan targets in Poland and Romania, the question was not of practical concern in the context of the GATT. In Hungary, however, with its more decentralized economic framework and its claim that tariffs constitute the main protective element, exploitation of monopoly and monopsony power on the domestic market was of importance to the GATT countries.

Efforts were undertaken in Hungary to abolish monopoly power. First, Hungarian authorities reimposed profit control on enterprises that showed an excessively high profit. This method was unsuccessful because it was difficult to know which gains were due to the efficient operation of the enterprise and which to monopolistic practices. Secondly, in certain cases the central Hungarian authorities directly fixed prices at a level which did not allow a monopolistic gain. Finally, the Hungarian authorities tried to limit monopoly power by breaking up large production and trade units and forbidding agreements between enterprises which would limit competition.

It is certainly true, though that the operation of monopolies considerably reduced competition on the Hungarian market.¹⁷ This problem is of particular importance in the context of the Hungarian tariff-based participation in the General Agreement.

TRADE CONTROL

QUOTA AND LICENSING

In all CMEA countries foreign trade is subject either to global or

individual licences.¹⁸ A licensing system that is country- or commodity-specific may influence the level of trade and introduce discrimination.

In Hungary, the overwhelming majority of imports, both from the centrally-planned and market economies, were transacted under global licences.¹⁹ In Poland and Romania the licensing systems relied, to a greater extent, on individual licences which referred to concrete transactions with a given country. In both countries the licensing system was more country-specific for trade with the centrally-planned economies than for trade with the market economies. Even under general targets and quotas, foreign trade could be channelled to conform with existing bilateral payments and trade agreements, by granting licences for imports and exports to one country while refusing them to another. Thus licensing presented an opportunity for discrimination. This was certainly the case with the Hungarian licensing system, and appeared also to be true of that of Poland and Romania, whereby individual licences were used to implement the country-specific allocation of products.²⁰

The only explicit quantitative restrictions applied in the Hungarian licensing system to imports originating from the market economies were global quotas for industrial consumer goods and several other products.²¹ They amounted to less than 5 per cent of total Hungarian imports from the convertible-currency area.²² Quotas for consumer goods were not broken down by commodity or country. As for Hungarian trade with the centrally-planned economies and the whole of Polish and Romanian foreign trade, restrictive plan targets maintained imports below free-trade level. Within these quantitative constraints, and in observance of the existing bilateral agreements, licences were issued in the three countries according to order of application, with no further prejudice towards particular partners.

As the Polish and Romanian licensing systems relied to a considerable extent on individual licences they required special attention in the GATT. It was the protective dimension of Hungarian quotas that would retain the interest of its GATT partners.

CUSTOMS TARIFFS

In Poland and Romania, goods imported or exported by foreign trade enterprises were not subject to customs tariffs.²³ Customs operations consisted merely of checking the goods against the accompanying documents. Tariffs were applied only to part of the imports and exports affected by private persons. In both countries tariffs were thus an ineffective instrument of trade control.

The new economic system introduced in Hungary in 1968 created conditions which permitted the introduction of effective tariff control.

Hungary, when acceding to the GATT, claimed that the importance of tariffs in her foreign trade system was comparable to that of the Western members of the GATT. The Hungarian customs tariff was based on the Brussels Tariff Nomenclature and, like the tariffs of other GATT countries, it was categorized into three columns. One was for goods originating in countries to which Hungary granted preferential treatment. The preferential tariff rate was applied for products from developing countries that did not discriminate against Hungary and had a *per capita* income lower than Hungary's.²⁴ The second column was for goods originating in countries to which Hungary granted MFN treatment. More than 90 per cent of total Hungarian imports were transacted under the second-column rate, even before Hungary's accession to the GATT. The third column of tariff rates applied to products from countries which did not accord MFN status to Hungarian exports. The average retaliatory rate was about twice as high as the average MFN rate. (A separate customs tariff applied to goods imported or exported by private persons.)

Hungary's tariff rates were fixed in relation to internal prices. At the time of Hungary's accession to the GATT, the tariff rates of the second column averaged approximately 30 per cent. The rates for raw materials ranged between 0 and 5 per cent, for semi-manufactures between 5 and 20 per cent, for manufactures and consumer goods between 40 and 50 per cent.²⁵ As in other economies the tariff rate was thus low on raw materials and higher on finished goods, which meant that the effective rate on the production process exceeded the nominal rate.

In addition to its customs tariff, Hungary maintained a system of turnover taxation. Turnover taxes were payable on goods and services sold to consumers regardless of whether the goods were domestic or imported. Hungary applied the import turnover tax only to imports from the centrally-planned economies. The tax was maintained in order to ensure that goods imported from the market economies sold for the same prices in Hungary as goods originating in the centrally-planned economies.

Although the Hungarian customs tariffs were basically applicable to all dutiable goods imported from market economies, there were some exceptions to this rule – in the form of so-called customs quotas, permit-slip procedure, and suspension of tariff rates.²⁶ These exceptions, however, were not of great quantitative importance.²⁷

In conclusion, when Poland and Romania acceded to the GATT they were not using tariffs as an instrument of protection or discrimination. In Hungary, the tariff system generally conformed with the non-discriminatory requirements of the GATT, but such exceptions as customs quotas, permit-slip procedure and the suspension of tariff rates required special attention.

EXCHANGE RATES

There are three exchange rates in Hungary, Poland and Romania. First, there is an official exchange rate. Official exchange rates are not equilibrium exchange rates and have no influence on the trade level. In Poland and Romania they serve primarily as units of account. By multiplying the foreign price of an imported product by the official exchange rate, one obtains the lei (Romania) or zloty (Poland) foreign currency price of the product. The lei or zloty foreign currency is a unit of calculation which makes it possible to reduce prices, tariffs and values, expressed in various foreign currencies, to a common denominator.

Secondly, there is the tourist exchange rate, set at a level which, on an average, does not significantly over-price goods and services normally bought by tourists. A special tourist rate, different from that used for commercial transactions, was introduced because in Hungary, Poland and Romania there existed a double-price system where consumer goods had higher prices than producer goods—even for identical products.²⁸

The third exchange rate is referred to as the commercial exchange rate. In Hungary, Poland and Romania, the profitability of a foreign trade transaction is determined by the relation between the domestic and foreign prices. The exchange rate used for this calculation is the same for exports and imports of all products. This differentiates, however, between the non-convertible currency area for Hungary and Romania, and between the centrally-planned economies, market economies and developing countries for Poland. After Poland's accession to the GATT, the same differentiation as existed in Hungary and Romania was adopted. The different exchange rates for the three countries are listed in Table 4.1.

Differentiation between the dollar and the rouble commercial exchange rates in Hungary, Poland and Romania was necessary because of the inconvertibility of CMEA currencies. This meant that exports to the market-oriented economies were valued at less favourable commercial exchange rates than those adopted for trade relations with CMEA countries. Since the commercial exchange rates in Hungary, Poland and Romania were considerably overvalued against the dollar, imports from the market economies were discouraged. In addition, the commercial exchange rate had a favourable effect on the expansion of Hungarian exports to the Western economies. In order to maintain a balance-of-payments equilibrium, in view of the overvalued exchange rates *vis-à-vis* the dollar, subsidies on exports and import restrictions were required in Hungary, and equalization systems had to be maintained in Polish and Romanian foreign trade. In Hungary and Romania, and from 1970 in Poland, there was practically no exchange-rate differentiation within the convertible currency area.

TABLE 4.1
Exchange Rates of Hungary, Poland and Romania (1970)^a

	Monetary unit	Gold content per unit	Official ex. rate in \$	Tourist ex. rate in \$	Commercial ex. rate in \$
Hungary	Forint	0.075758	11.74	30.00	60.00
Poland	Zloty	0.222168	4.00	24.00-40.00	70.00
Romania	Lei	0.148112	6.00	12.00-18.00	20.00 ^b

^a Tourist exchange rate and official exchange rate indicated according to: R. J. Hamilton, *East-West Trade and Payments Relations*, IMF Staff Paper (Washington: IMF, January 1970) p. 184.

^b Refers to 1973, *Instruction No. 76* (Bucarest: Hungarian Ministry of Foreign Trade, Ministry of Finance, December 1973).

Transactions concluded by Hungary, Poland and Romania with the market economies were settled mainly by cash payments in convertible currency, usually sterling or dollars. Other methods of payment used were credit, barter and switch deals. In Poland and Romania convertible currencies, as well as import licences, were available to importing enterprises, in accordance with foreign trade plan targets. In Hungary, enterprises that obtained an import licence and had the necessary amount of domestic currency were no longer obliged to apply for a separate foreign-exchange allocation.²⁹

In Poland and Romania, in order to encourage producers and consumers, foreign-exchange funds, to be used for additional imports required in the production process and for investments, were allocated to the branch ministries and to those associations and enterprises which exceeded the export targets. These foreign-exchange funds were valued according to additional export or import savings.³⁰ No retention of foreign exchange by domestic enterprises was permitted in Hungary.³¹ Approximately 70 per cent of Hungarian, Polish and Romanian trade with non-CMEA countries was conducted on the basis of convertible currency. Among countries that traded with Hungary, Poland and Romania under bilateral payments agreements, Austria, Finland, Greece, India and the United Arab Republic accounted for the major shares.

The exchange rate, used in Hungary, Poland and Romania by the foreign-trade enterprises, was the commercial exchange rate which could influence the level of trade only within the framework of the multi-commodity and one-commodity targets; its impact on the level of trade was thus limited. Because they differentiated between two areas, however, they caused discrimination. This discrimination could be justified by the existence of two currency areas. In Hungary, in addition to its discriminatory role, the commercial exchange had a much more important impact on the level of trade in relations with the market economies.

SUBSIDIES

Under Polish and Romanian target control, exports could be increased above the free-trade level and imports could be restricted. Since the domestic price level was maintained above the level of world prices, when the two were compared at the commercial exchange rates, Polish and Romanian enterprises usually made a profit when they imported and suffered a loss when they exported. In order to turn the importer's profit over to the state and to offset the exporter's loss out of the state budget, a system of price equalization was maintained in Poland and Romania.³²

Under the one-commodity targets, trade was determined by these

targets, and the equalization system as practised in Poland and Romania could not be considered subsidizing in the GATT sense. The negative tax, however, calculated by a planner *ex ante* for an n-commodity target, owing to changes in trade conditions, could become a subsidy in the GATT sense.

It may thus be concluded that in Poland and Romania budgetary payments for foreign trade enterprises were of a double nature: on the one hand, they resulted from a direct allocation of trade through plan targets under given prices; and on the other hand, they influenced the level of exports on certain products within the framework of multi-commodity targets – to this extent they somewhat resembled a subsidy in the GATT sense.³³

Subsidies as effective measures of trade control were applied in the Hungarian system of trade control for exports to the market economies. At the time of Hungary's accession to the GATT, they were being paid on a sector basis rather than a product basis, and they were made public by the Hungarian authorities. The granting of subsidies for about two-thirds of Hungarian exports resulted primarily from over-valuation of the forint. Subsidies were considered temporary measures, adopted to safeguard the balance of payments after the introduction of the 'new economic mechanism' and to permit some enterprises to shift progressively from their unprofitable product-mix to more profitable production.³⁴ Subsidies were not supposed to result in dumping but rather to eliminate the difference between the domestic and foreign prices when compared at the commercial exchange rate (which was not an equilibrium exchange rate).

A problem closely related to subsidies and the equalization system was that of export price formulation. Under the price systems in Poland and Romania, export prices were not automatically based on the cost of production or the domestic market price. However, Polish and Romanian planning authorities who set targets, and foreign trade enterprises that exported, sought to obtain normal economic advantages from export transactions, in accordance with market conditions and without upsetting world market prices. According to domestic regulations, trade enterprises were obliged to export at prices prevailing in foreign markets. It was also in their financial interest to do so because their activities were based on profit principles.

It is often claimed in Western countries that the East European monopolies tend to dump on Western markets. The issue is a highly controversial one. Both monopolistic traders and state-owned trade enterprises are typical of the foreign trade systems of Eastern Europe. It could thus be claimed that the known economic arguments for long-term dumping, (i) based on discriminatory monopoly power or (ii) implemented through state trading, are particularly relevant to East European exports.³⁵ Moreover, East European management of foreign

trade often lacks flexibility in the context of changing foreign prices and domestic production cost, which in turn increases the risk of short-term dumping on Western markets.

The GATT experience, however, in respect of dumping in East-West trade, does not contradict the East European claim that dumping by East European products is due to exceptional situations. To date, in fact, only a few cases of dumping have been proved against East Europeans under the GATT.³⁶ East European governments have also claimed in the GATT that their export prices are fixed at the world price level; but when it has been found to be difficult to determine such prices, they have been fixed at prices comparable with those of third-country suppliers.

Nevertheless, the problem of East European products being dumped on the Western markets remains the subject of anxiety on the part of some Western producers. Balance-of-payments deficits among East European countries *vis-à-vis* the West and a tightness in their primary production sectors has resulted in an intensification of East European efforts to export standard manufactures and services to the Western area. Hugh Corbet, of the Trade Policy Research Centre, in London, has rightly noted that these developments might bring about a weakening of the liberal trade coalition of interests in the West, not only in respect to East-West trade but to trade in general, as a consequence of claims by domestic producers in Western markets that imports of East European products are being dumped or subsidized.³⁷ The issue, therefore, requires careful consideration in the GATT.

PRICE FORMATION

In Poland and Romania, domestic prices were for the most part centrally fixed and re-examined by central or local authorities. In a limited number of cases, cooperative bodies and enterprises might fix the prices of their products. From the standpoint of resource allocation and the requirements of intensive economic growth, these prices were not rational. Neither were they equilibrium prices. It could not be assumed that prices bore the same relationship to each other as they would when in a state of equilibrium. Within the limits of the obligatory targets, prices had a certain allocative function and thus could bring about product discrimination. The allocative function of price formation in the foreign trade sector, however, was of little practical significance to the GATT, due to the maintenance of targets, individual licensing and the existence of the equalization mechanism.

Domestic prices in Poland and Romania were generally based on average costs excluding interest but there was substantial deviation from this rule. The complicated system of taxes and subsidies resulted in a duality of the price system: on average, consumer prices were higher

than producer prices, even for the same or similar products. Although the prices for certain agricultural products and services which were considered essential by central authorities were kept low, for social and income distribution reasons, prices of light industrial products were relatively high, and prices of luxury items (for example, cars, coffee, chocolate and oranges) were very high. The product discrimination implemented by the Polish and Romanian authorities was reflected in price relations, and could engender country discrimination against the tropical developing countries exporting food stuffs, for example.³⁸

In Poland and Romania prices of imported products were fixed at a level at which these goods would sell. The principles of price formation were the same for commodities imported from the market-economies as they were from the centrally-planned economies. Imported products destined for consumption were subject to the same turnover taxes and other charges as the corresponding domestic products. Some differences between prices of imported products and prices of domestic products could be attributed to differences in quality or to the fact that the foreign products were qualified as luxury items.

Polish and Romanian authorities had no interest in importing goods merely to augment stock. In the event that the price of a product was found to have been fixed too high, an adjustment would certainly be made. When the foreign exporter wanted to have a say in determining the price at which his product would be sold on the Polish or Romanian market, the supplier might make inquiries in advance and ascertain the retail selling price. Introduction of economic reform in Hungary (1968) opened the way to market relationships among domestic enterprises, and prices assumed an allocative function.

Three categories of prices existed in Hungary: fixed prices, prices adjusted in conformity with official regulations, and free prices. Free prices covered approximately 30 per cent of the total.³⁹ Furthermore, the central authorities had the power of veto over price increases for certain goods. These goods accounted for 5 to 8 per cent of industrial production. Indirect price control was also possible through limitations on profits in the case of commodities traded under agreement between buyer and seller. Fixed prices were maintained in order to (i) support particular production branches for the promotion of development objectives (subsidies); (ii) to avoid inflation in some commodity groups (a vast range of consumer products in short supply); and (iii) for public health, cultural and income policy reasons. The majority of fixed prices thus deviated from prices that would normally result from production costs and market conditions. Centrally-fixed producer prices were equated to average rather than marginal cost, which gave rise to distortions, particularly in raw materials and semi-manufactures. In this case a weighted average of home-produced and imported materials served as a basis for calculation.

The Hungarian price reform brought the fixed and free prices of consumer goods nearer to producer prices. The number of turnover tax rates was reduced to about 500. Due to the operation of the turnover and differential tax system, however, consumer prices were still about 20 per cent higher than producer prices for industrial products and about 20 and 12 per cent lower for food and transportation, respectively.

The Hungarian price system ensured a close relationship between foreign and domestic prices.⁴⁰ For investment and producer goods, the foreign price of the imported commodity was converted into domestic currency by means of the commercial exchange rate and the customs tariff. What is more, in the case of consumer goods the turnover tax, the marketing expenses and the income margin of the domestic trader had to be taken into consideration.⁴¹

All manufactured consumer goods imported from market economies, and the majority of other imports were in the free-price category.⁴² The Hungarian domestic tax system did not discriminate between imported or domestically produced goods: the price components for imported goods were the same for every product, whether or not the product was also manufactured at home or was obtainable from CMEA or market economies.⁴³

This 'liberal' image of the Hungarian price formation, however, requires certain qualifications. First, due to the limitations on imports of most finished goods and especially consumer goods, domestic producers often had a monopoly position without fear of competition from imports. Secondly, central price control of raw materials in Hungary resulted in different treatment of raw materials according to area of origin. As a rule, the prices of raw materials imported from CMEA countries were lower than those of products originating in the Western economies.

DISCRIMINATORY TRADE ARRANGEMENTS

BILATERAL TRADE ARRANGEMENTS WITH MARKET ECONOMIES

Bilateral trade arrangements maintained between Hungary, Poland, and Romania, on the one hand, and market economies, on the other, took a variety of forms. For many years after World War II, bilateral payment arrangements were most frequently used for bilateral trade between Hungary, Poland and Romania, and the market economies. Due to the high degree of bilateralism, prices in East-West trade often diverged from world prices.

Western exporters were unwilling to sell at world prices under barter trade for payments in commodities of lower quality, which often had to be resold by the intermediary of switch houses to Western consumers

(the switch houses charged 25 per cent and more). On the other hand, the East European countries, often under the pressure of deficit barter arrangements, were forced to export to the Western markets at prices 5 to 10 per cent below world prices.⁴⁴

In the mid-1950s, Poland and Romania maintained bilateral payment agreements with their most important Western partners. The number of these agreements was considerably reduced in the following years. Moreover, from 1957 on, the multilateral compensation procedure existed, organized under the auspices of the Economic Commission for Europe (ECE). This made it possible to turn some bilateral balances into convertible currency through a switch operation after the subtraction of a certain discount. However, up until 1968, only ninety-one compensation circuits, comprising 348 links, with a total value equivalent to \$134.2m, had been arranged. This indicates the relative unimportance of the scheme.⁴⁵

In spite of the reduction of a number of bilateral payment arrangements concluded by the three East European countries with the developed market economies, there was still an increasing number of such agreements with the developing countries (see Chapter 6).

Another form of East-West arrangement for bilateral trade consisted of agreements by which the centrally-planned economy made an import commitment in return for the allocation of an import quota by the market economy. These agreements were usually initiated by the market economies in order to assure certain trade levels to substitute for the guarantee of equality of trading opportunity. Traditionally, they covered all the trade flow between partner countries, including a long commodity list which might constitute a licensing commitment for the centrally-planned economies. The products listed in the agreement were negotiated annually by the partners. Sometimes they were supplemented by enumeration of trade in large industrial projects and extension of government credit facilities. Import commitments undertaken by the centrally-planned economies under these arrangements were usually discussed with the relevant domestic producers and foreign trade units. Specification of purchases was often relatively easy, since imports from the industrialized market economies consisted mainly of large 'package transactions'—important investment equipment or producers' materials—where source of supply and value of transaction could be easily estimated a year in advance. To some extent this annual setting of import commitments for certain products under bilateral trade agreements could be considered an inter-state projection of important contracts negotiated by economic units.

With the liberalization of East-West trade, the form of these bilateral agreements changed considerably. Commodity lists became shorter and import commitments referred to a wider range of products. Often they dealt with other more general issues—such as the MFN clause, mutual

financing arrangements, clauses on arbitration and safeguards against dumping and market disruption. The bilateral agreements rarely provided for compulsory trade; rather they estimated quotas which were either indicative or merely the stated requirement to issue the necessary licences based on previously signed contracts. Poland and Romania maintained only a few arrangements of this type with the market economies. Under the system adopted by Hungary for trade with the market economies, the central administration gave no orders to Hungarian enterprises to import particular products. In a few cases only import commitments were agreed upon in bilateral trade agreements. They referred, however, exclusively to goods and quantities determined previously by contracts on the enterprise level.⁴⁶

There were also agreements concluded by Hungary – and to a lesser extent by Poland and Romania – with the market economies, explicitly providing for the preferential treatment of a particular country. Hungary granted, for example, tariff facilities within the production cooperation contracts to some Western economies. Some agreements provided, as well, for the abolition of quantitative restrictions or exemption from taxes when supplies of goods agreed upon were concerned.⁴⁷

Poland and Romania in several cases undertook bilateral obligations involving the issue of licences. Since, in other cases, these licences might have been refused, obligations of this kind amounted to a preferential licensing policy. It should be noted, however, that preferential treatment, as agreed upon by Hungary, Poland and Romania in some arrangements, usually in connection with industrial cooperation agreements, involved only an insignificant share of trade – 3 per cent of Hungary's trade with the market economies and even less for Poland and Romania.

In spite of the increasing trend towards multilateralism, the trade relations of Hungary, Poland and Romania with those developing countries who were members of the GATT continued to be based, to a considerable extent, on bilateralism. Even broader moves towards multilateralism were required if the spirit of the GATT on multilateral and non-discriminatory trade was to be respected in relations with the East European members of the General Agreement.

TRADE ARRANGEMENTS WITH CENTRALLY-PLANNED ECONOMIES

The duality of the Hungarian and, to a lesser degree, of the Polish and Romanian trade control systems, along with the specific character of their trade with other centrally-planned economies, poses the question of discrimination between the market economies and the centrally-planned economies.

Hungary, Poland and Romania are members of the CMEA, and

intra-CMEA trade accounts for an important part of their foreign trade (see Table 4.2).⁴⁸

TABLE 4.2
Area Composition of Imports of Some CMEA Countries
(per cent share)

Country	Year	CMEA	Developed market economies	Developing countries	Other
Hungary	1960	64.6	24.7	4.4	6.3
	1965	64.5	25.5	7.0	3.0
	1971	63.1	29.3	4.4	3.2
Poland	1960	58.1	29.7	6.8	5.4
	1965	61.7	24.5	9.4	4.4
	1971	64.1	27.4	5.3	3.2
Romania	1960	67.9	23.4	3.5	5.2
	1965	57.5	33.3	5.5	3.7
	1971	46.3	39.6	6.6	7.5

SOURCE: *Rocznik Statystyczny Handlu Zagranicznego*, 1972 (Warsaw, 1973) p. 76.

The intra-CMEA share of total trade for Hungary, Poland and Romania, however, is not excessively high when compared to the share of trade with neighbouring states for some developed market economies;⁴⁹ and, except for the Soviet Union, with which the former Hungarian, Polish and Romanian regimes had abolished all trade, that share closely parallels the situation before World War II.

It should also be noted that the CMEA is composed of a group of countries trading bilaterally under rigid targets and discriminating amongst each other. Despite the ambitious integration objectives, the rigid plan targets for intra-CMEA trade continue to emerge mainly from bilateral arrangements. More than 50 per cent of CMEA trade was subject to volume plan targets in the late 1960s; about 40 per cent was regulated by multi-commodity targets, and only 10 per cent was controlled by targets with no product specification.⁵⁰ Intra-CMEA targets often specified country of origin and destination of goods and in that sense were more discriminatory than targets for trade with the convertible currency area.

Maintenance of the mandatory foreign trade system within CMEA was due to the high degree of bilateralism in CMEA trade. This bilateralism, in turn, to a considerable extent resulted from the non-transferability of debts among the CMEA states. In 1964 efforts were made to improve this situation by setting up the International Bank for

Economic Cooperation (IBEC), which was expected to contribute to the equalization of the balances of the members states by granting swing credits and short-term advances from its funds. The deficit member countries, however, were neither required to pay their balances (not even partly) in convertible currency nor to pay sufficiently high interest rates on outstanding debts. Therefore surplus countries preferred to retain bilateral balancing of trade accounts, and until 1968 bilateralism was still increasing.⁵¹

From 1971 the situation improved when IBEC's interest rates rose to 5 per cent, making the holding of the Bank's funds more costly to debtors and more interesting to creditors. In addition, heavy sanctions were introduced for non-fulfilment of obligations as agreed upon in bilateral trade agreements. The persistent inefficiency of mutual compensation of clearing and credit policy, as practised by IBEC, resulted in bilateral balancing of trade accounts among CMEA members. The consequence of this was a high discrimination among CMEA partners. The CMEA appeared to be less a regional market (or an area subject to central foreign trade computation) than an assembly of fraction markets, where prices for comparable products could differ according to currency and contract. How was it, then, possible to consider the CMEA as a trade preference area?

On the one hand, CMEA members discriminated against outsiders by establishing intra-CMEA trade targets which were preferential when compared with the target quotas or tariffs hampering imports from outside CMEA. Michael Kaser, the British expert on East European economies, noted that this procedure had the same result as a customs union, though discrimination depended not on the common tariff wall but on the agreements to disregard outsiders' offers.⁵² On the other hand, markets of developed economies were separated from CMEA by a discriminatory (*de facto* or *de jure*) wall of quantitative restrictions. And there was still strategic control of certain exports to CMEA.

At this stage as well, the dissimilarity between the economic and social systems of the two areas accentuated the difficulties. Restricted information flow resulted in poor knowledge of market openings, and political tensions created an unfavourable climate for credit arrangements. Finally, the industry-oriented development pattern in Eastern Europe reinforced the export expansion of many East European countries to the CMEA area. While manufactured goods were a predominant part of Poland's and Hungary's intra-CMEA exports, these countries were relatively unsuccessful in selling machinery and other advanced products on the Western markets, partly because of difficulties in meeting Western technical requirements. The desire to transform the traditional structure of foreign trade and to shift from exports of food and raw materials to more industrially advanced goods committed export expansion to the CMEA and developing area.

Due to the separation of the CMEA market from the rest of the world, some particularly scarce products within the CMEA tended to be priced above the world price level.⁵³ Price preferences, once introduced in bilateral trading, are likely to bring about reciprocal price preferences. A rigid system of bilateralism forced some CMEA countries to purchase goods from their partners simply in order to balance exports. Some of these imports were eventually re-exported outside the CMEA and sold at even lower prices.⁵⁴ This tendency was reinforced by the lack of a compensation mechanism between the two areas.

The CMEA countries may claim that neither the CMEA Charter nor any other document explicitly provides for preferences in the group's trade. In fact, the coordination of national plans among CMEA countries in no way attempts to introduce supranational directive planning. Recommendations in that respect may be formulated only with the consent of all interested members. Their validity, like that of the decisions of the Council, do not extend to members who declare themselves uninterested in the matter. Moreover, the plan coordination is expected to be an organic part of the universal division of labour.⁵⁵

One of the most disturbing features of Hungarian, Polish and Romanian foreign trade is its possible anti-West discrimination. It is difficult to prove the existence of such discrimination in view of the different methods used in intra-CMEA trade, the lack of an explicit equilibrium exchange-rate system, and certain other political and economic characteristics of intra-CMEA commercial relations. The problem of intra-CMEA trade is certainly one of the most complicated issues touching the GATT membership of Hungary, Poland and Romania – for both technical and political reasons.

SUMMARY AND CONCLUSIONS

Hungary, Poland and Romania were state-trading systems. In its trading with the market economies, the Hungarian system could be classified as a loose state-trading system. The Polish and Romanian state-trading regimes, at the time of accession to the GATT, had characteristics of the command systems.

In Poland and Romania foreign trade targets distinguished between the convertible and the non-convertible currency area. They did not differentiate, however, between particular countries within the convertible area, and thus could be considered non-discriminatory. The Hungarian, Polish and Romanian state-trading enterprises were influenced by profit criteria; like private traders they were therefore naturally concerned with commercial considerations.

The limited participation of domestic economic units in the foreign trade sector, and the fact that some of these units enjoyed a monopolistic

situation on the Hungarian, Polish and Romanian markets, could raise doubts as to the degree of competitiveness of state trading in the three countries. The question was of most concern in Hungary, which claimed in the GATT that tariff constituted its main instrument of protection. In Hungary, Poland and Romania the most significant danger of discrimination against specific market economies came from the licensing system. The issue was of particular importance in Poland and Romania, where individual licences covered a large share of total trade.

When Poland and Romania joined the GATT, tariffs were not effective instruments of trade control; neither were they used as instruments of discrimination. In Hungary, where tariff constituted a main protective element *vis-à-vis* the market economies, the tariff system could be considered basically non-discriminatory towards countries granting MFN tariff treatment to Hungary.

Hungarian, Polish and Romanian exchange rates differentiated between the convertible and non-convertible currency area. But since they did not discriminate between particular countries of the convertible-currency area, they could be considered non-discriminatory within that area.

In Poland and Romania, equalization payments (*ex ante*) could not be considered subsidies in the sense implied by the GATT. Subsidies, however, were used in the Hungarian foreign trade system. Application of the Hungarian subsidies conformed for the most part with the provisions of the GATT.

Free price formation was especially important in Hungary in the context of the efficiency of the Hungarian tariff system. The Hungarian foreign trade system could be considered as largely based on free price formation and the existence of a direct link between domestic and foreign prices.

Polish, Romanian and Hungarian foreign trade with those developing countries, who were members of the GATT, was carried out to a great extent on a bilateral basis. A progressive move towards multilateral trading is required if conformity with the GATT principle of multilateralism is to be attained.

The special character of Hungarian, Polish and Romanian trade relations with the CMEA and the anti-West discrimination (which in the opinion of some economists characterized CMEA) could be expected to become one of the most disturbing features of the three countries' accession to the GATT.

NOTES AND REFERENCES

1. Bela Csikos-Nagy, 'Incidence de la réforme économique sur le commerce extérieur hongrois', *Revue de l'Est*, Paris, October 1970, p. 12. For the

- Hungarian definition of 'state monopoly of foreign trade' see also GATT Doc. L/3301, January 1970, p. 19.
2. Harriet Matejka, *Trade Control in Eastern Europe*, a study which is not yet published.
 3. Export targets usually indicated only the minimum trade flows; and they could be exceeded.
 4. A plan target may determine a quantity of imports that would result in a difference between domestic and foreign prices. This difference is referred to as an implicit tax.
 5. GATT Doc. L/3301, January 1970, pp. 19–21 and 29.
 6. Jozef Siebeneichen, 'Planowanie obrotow towarowych w polskim handlu zagranicznym', *Handel Zagraniczny*, Warsaw, May/June 1968, pp. 204–7.
 7. Witold Trzeciakowski, 'Evolution de la planification et de la gestion du commerce extérieur en Pologne', *Revue de l'Est*, January 1971, pp. 5–37.
 8. *Ibid.*, pp. 29–32.
 9. The Polish and Romanian memorandum on foreign trade regime as presented in the GATT explicitly recognized that the Ministry of Foreign Trade could 'draw the attention' of the foreign trade enterprises to certain developments related to foreign trade.
 10. *Economic Bulletin for Europe* (Geneva: United Nations, 1973) vol. 24, no. 1, Table 1.
 11. Beginning on 1 January 1971, the majority of Polish foreign trade enterprises came under the administration of ministries responsible for the different branches of industry. In Romania the industrial associations undertook important functions in foreign trade.
 12. GATT Doc. L/3301, January 1970, p. 21.
 13. *Ibid.*, p. 20.
 14. GATT Doc. L/3426, September 1970, p. 31.
 15. For example, in Poland the DAL corporation maintained its own import-export houses in India, Nigeria, Venezuela and Lebanon, and operated outside the annual foreign trade and currency plan.
 16. GATT Doc. L/3211, May 1969, p. 10.
 17. Bela Balassa, 'The Economic Reform in Hungary', *Economica*, London, February 1970, pp. 1–22.
 18. Global licence permits conclusion of the transaction specified in the licence with any country, meaning it is not country-specific. The individual licence refers to a concrete transaction – it means defining the import or export value of a given product with a given country and under established conditions.
 19. GATT Doc. L/3301, January 1970, p. 20.
 20. *Economic Survey of Europe in 1968* (New York: United Nations, 1969) p. 102. In many bilateral agreements for example, Poland and Romania included a clause that licences would be issued on trade with the country party to the agreement.
 21. Electrical energy, automobiles, foundry equipment, furnaces, coke and fertilizers; see GATT Doc. L/3426, September 1970, p. 18; and GATT Doc. Spec. (71) 1, January 1971, p. 30.
 22. GATT Doc. Spec. (71) 1, January 1971, p. 39.
 23. The situation has changed lately; see Chapter 6.
 24. GATT Doc. Spec. (71) 1, January 1971, p. 14.

25. GATT Doc. L/3301, January 1970, p. 29.
26. In 1969 about thirty customs quotas were accorded in Hungary.
27. Lists of goods that might be subject to the tariff concessions (permit-slips) and tariff quotas were published in the official journals. In 1969 tariff concession procedures and duty suspension was applied to about 5m forints worth of imports, less than 1 per cent of Hungarian imports from the market economies.
28. As a rule, in the majority of economies, the ratio of purchasing power parities to exchange rates is a function of disparities in *per capita* incomes. Thus the exchange rate usually exceeds the purchasing power parity (0.78 in the French-United States relationship and 0.63 in the Japanese-United States relationship, to give two recent examples). Balassa, 'The Purchasing Power Parity Doctrine: Reappraisal', *Journal of Political Economy*, Chicago, February 1964, pp. 584-96.
29. GATT Doc. L/3301, January 1970, p. 45.
30. GATT Doc. L/3211, May 1969, p. 21.
31. GATT Doc. L/3426, September 1970, p. 16.
32. Under these equalization systems the state bank accounted the export revenue and import expenses of the foreign trade enterprises at the official exchange rate. Since this rate was not an equilibrium exchange rate, disparities appeared between the export revenues and import expenses converted at that rate and their value when accounted at domestic prices. The price equalization system compensated for these differences.
33. Compare: Model II of command state-trading in Chapter 3.
34. *Economic Survey of Europe in 1968*, *op. cit.*, p. 102.
35. Indeed, the monopolistic exporter facing less elastic demand at home than abroad may restrict domestic supply and raise the domestic price over the export price. Similarly, in the case of a state-owned exporting unit induced to stimulate exports or provide protection to domestic producers, rather than maximize profit, a high price charge at home may provide income to subsidize exports. For a more detailed analysis, see W. M. Corden, *Trade policy and Economic Welfare* (Oxford: Clarendon Press, 1974) pp. 235-47.
36. Poland was accused only twice of dumping during its membership of the GATT, and only one case was proved. See Josef Wilczynski, *The Economics and Politics of East-West Trade* (New York: Praeger, 1969) p. 187. See also Chapter 6.
37. Hugh Corbet, 'Britain's Predicament in the Struggle for an Open World Economy', in Corbet, Corden, Brian Hindley, Roy Batchelor and Patrick Minford, *On How to Cope with Britain's Trade Position*, Thames Essay No. 8 (London: Trade Policy Research Centre, 1977) pp. 22-3.
38. Frederic Pryor, 'Trade Barriers of Capitalist and Communist Nations Against Foodstuffs Exported by Tropical Underdeveloped Nations', *Review of Economics and Statistics*, Amsterdam, November 1966, pp. 406-11.
39. Fixed or maximum prices were maintained for about 70 per cent of agricultural products and domestically produced materials and semi-manufactures, 50 per cent of consumer goods and services and about 20 per cent of industrial end-products. See: Balassa, 'The Economic Reform in Hungary', *op. cit.*, p. 11.
40. The automatic link of domestic and Western prices was still somewhat restricted by the use of quotas, licensing and targets.

41. GATT Doc. L/3301, January 1970, p. 13.
42. GATT Doc. L/3426, September 1970, p. 23 and GATT Doc. Spec. (71) 1, January 1971, p. 1.
43. GATT Doc. L/3426, September 1970, p. 28.
44. Holzman, 'More on Soviet Bloc Trade Discrimination', *Soviet Studies*, Glasgow, July 1965, p. 52.
45. *Eleventh Annual Report on the Operation of the Multilateral Compensation Procedure*, E/ECE/712, (Geneva: July 1968).
46. GATT Doc. L/3426, September 1970, p. 6.
47. *Ibid.*, p. 31.
48. Besides Hungary, Poland and Romania the following countries are CMEA members: Albania (non-active member), Bulgaria, Cuba, East Germany, Mongolia, the Soviet Union and Yugoslavia (associate member).
49. In 1970 the share of imports from neighbouring countries in total imports amounted to: 61.5 per cent for Austria, 57 per cent for Belgium and Luxembourg, 51.5 per cent for Denmark, 45.1 per cent for France, 70.3 per cent for Canada, 56.4 per cent for Switzerland.
50. Tibor Kiss, *International Division of Labour in Open Economies with Special Regard to the CMEA* (Budapest: 1971) p. 171.
51. H. Francuz, 'The International Bank for Economic Cooperation', *IMF Staff Papers*, Washington, November 1969, pp. 489–503.
52. Michael Kaser, *COMECON, Integration Problems of the Planned Economies* (Toronto: Oxford University Press, for the Royal Institute of International Affairs, 1965) p. 143.
53. Stanisław Polaczek, 'Problemy systemu cen w handlu między krajami socjalistycznymi', *Gospodarka Planowa*, Warsaw, August–September 1967, pp. 45–6.
54. For example, Hungary's re-exports were estimated at 12 per cent in 1955. See Alan A. Brown, 'Towards a Theory of Centrally Planned Foreign Trade', in Brown and Neuberger (eds), *International Trade and Central Planning*, *op. cit.*, p. 87.
55. 'Basic Principles of International Socialist Division of Labour', *New Times*, Moscow, no. 27, 1962, pp. 33–40. The open character of the CMEA has been also confirmed in the CMEA integration programme adopted in 1971.

Mechanics of East-West Trade in the GATT

The GATT, as shown in Chapter 3, was drafted for market economies, controlling their trade essentially by means of price-mechanism devices, and resorting to state trading only occasionally. Its provisions could therefore be expected to apply only with difficulty to Eastern European state-trading economies controlling their trade by means of plan targets, especially in view of the GATT principles of non-discrimination and reciprocity and to the GATT rules on integration. Chapter 4, however, showed that while the economic systems of Poland and Romania at the time of accession were centrally-planned and geared to state trading, Hungary's was a state-trading system in the process of introducing price-mechanism devices to which the GATT provisions could, therefore, be expected to apply fairly readily.

This chapter examines the accession to the GATT of Poland, Romania and Hungary and the solutions found to the problems their membership raised. It concludes that both the reciprocity formula adopted for Poland and Romania and the GATT mechanism for assuring non-discrimination in East-West trade suffer from important weaknesses.

RECIPROCITY

RECIPROCITY BETWEEN TARIFF- AND TARGET-PROTECTED ECONOMIES

Basically, the problem of finding a reciprocity formula for trade with the target-protected economies could have been approached in two ways: exchange of tariff reduction by the tariff-protected economy for import expansion on the part of the target-protected economy; or explicit provision for exchange of tariff reduction for a commitment to reduce level of protection.

The first solution had proved to be realistic in the past. The earliest

examples of this type of reciprocity arrangement were the bilateral trade agreements concluded by Soviet Russia with some market economies in the 1920s. The reciprocity formula provided for tariff concessions by the Western governments in exchange for import commitments from the target-protected economy. These arrangements were usually supplemented by safeguard clauses that provided for a right to suspend application of the tariff reduction if the target-protected economy failed to make the purchases envisaged.¹

The first attempt to extend this bilateral reciprocity formula to a multilateral framework was contained in the American 'Suggested Charter'. The authors of the Charter toyed with the idea of introducing a 'global commitment' clause under which a target-protected economy would negotiate its purchasing plan periodically with the tariff-protected economies. Tariff reduction on the multilateral side was thus expected to be exchanged for a global import commitment on the side of the target-protected economy. This solution also influenced the provisions of the Havana Charter on state monopolies.

A similar concept underlay the proposals formulated in the late 1950s, when the problem of East-West trade aroused new interest. Three of those proposals were of particular significance for our present discussion.

In 1958, a Swedish diplomat, C. H. von Platen suggested East-West trade should be expanded by admitting East European products to Western markets under the same rules as those from OEEC countries. In exchange the East European economies were 'to increase their total trade with Western partners (or the currency area of these partners) by a certain average annual percentage'.² The scheme proposed a reciprocity formula of a multilateral character. The formula was asymmetric as to both the nature of exchanged concessions and their degree of specification.

Two years later, Professor Jacques L'Huillier, from the University of Geneva, proposed that better access of the East European economies to the Western market should be exchanged for an East European commitment to buy specific categories of products equal in value to their intended (planned) exports to the West.³ The project implied an asymmetric formula where item-by-item concessions of the target-protected economies would be exchanged for item-by-item concessions of the tariff-protected economies. Moreover, the formula emphasized the balance-of-trade criterion of reciprocity, since it provided for the equalization of imports and exports between the target-protected economy and the multilateral trade area in the West.

A different idea for the reciprocity of trade between the tariff-protected and target-protected economies was developed by the GATT Secretariat in the late 1950s, when Hungary and Poland showed interest in accession to the General Agreement. Eric Wyndham White, as

Secretary General of the GATT, suggested that since some assurance was required concerning the mark-ups on the resale of market-economy products in the target-protected economies, the level of such mark-ups should be negotiated in much the same way as tariffs were negotiated under the GATT. In other words, the proposal provided for an asymmetric formula in which a tariff reduction was exchanged for a commitment to reduce the level of protection through concessions on the mark-ups. The exchanged concessions were expected to have an item-by-item character. Where such negotiations were impracticable or unsatisfactory, however, it was suggested that a solution based on import commitments by the target-protected economy be adopted.⁴

The problem of an East-West reciprocity formula was raised several times during discussions in the United Nations. It was agreed that effective reciprocity in East-West trade should be achieved by means of a realistic and practical approach. The following recommendation was made. 'Effective reciprocity/mutual advantage should be measured in terms of concrete and comparable results, i.e. the increase in the volume and composition of trade between countries with different systems which would satisfy the trading partners.'⁵

This recommendation would seem best satisfied through an import expansion commitment from the target-protected economies for particular groups of products.

POLISH RECIPROCITY FORMULA

Poland's participation in the GATT provided the first occasion where a multilateral reciprocity formula for trade relations with a target-protected economy could be used. Initially, Poland desired a reciprocity formula based on her import commitment in respect to certain goods. Two main proposals were discussed.

The first proposal provided for the establishment of a Polish import commitment through negotiations on an item-by-item basis. The Polish Government suggested that the initial negotiated import level should be established through a representative period approach. Its partners, however, were assured that the approach did not exclude the possibility of establishing new import rights to the Polish market. In the Polish view, allocation of the imports by country should either take place during negotiations or be regulated by some scheme like tenders. The suggestion was rightly refused on the grounds that it conflicted with the GATT principle of non-discrimination, banning country-specific direct trade control. Instead, it was decided that any interested enterprise from the GATT countries might compete for the Polish market; it would then be up to the Polish import unit to choose the most advantageous offer according to normal commercial practice.

The suggested formula relied thus on item-by-item concessions. To

this extent, it conformed with the general reciprocity practice of GATT countries before the Kennedy Round. The formula was also expected to include negotiations on Polish plan targets which were to be reported in advance. This aspect of the proposal was in line with the GATT reporting requirements on quotas. It was, however, opposed by Poland in subsequent discussions.

The second formula suggested for Poland's participation in the Kennedy Round provided that:

Increased export earnings obtained by Poland as a result of tariff cuts or elimination of other barriers to her exports to the contracting parties will be used to increase her imports from the contracting parties in proportions and on the conditions to be agreed upon.⁶

It was supposed to be achieved by the intermediary of a 'special fund' consisting of savings from import duties which would be used for additional imports. The exact proportion of these savings, which should be reflected in increased imports to Poland, would be subject to negotiations. Poland was also expected to agree with interested members of the GATT to include certain categories of goods in its import plans or to secure for certain imports a percentage increase higher than that for average Polish imports.⁷

Thus the project provided mainly for exchange of linear concessions with item-by-item bargaining reserved for exceptional cases. To this extent the suggested formula was in conformity with that of the Kennedy Round negotiations. The proposal strongly emphasized the balance-of-trade criterion for reciprocity and to a country like Poland, under continuous balance-of-payments pressure, this was of no minor importance.

The formula finally agreed upon for Poland in the GATT, provided that, in return for tariff reductions by the GATT partners, the Polish Government would undertake to:

increase the total value of its imports from the territories of contracting parties by not less than 7 per cent per annum.⁸

It further explicitly noted that the GATT countries might conclude with Poland:

agreement on Polish targets for imports from the territories of the contracting parties as a whole in the following year.⁹

The formula, therefore, is based on the exchange of Poland's import commitment for tariff concessions from partner countries. The formula

is basically general, providing for the exchange of linear concessions. Nevertheless, item-by-item negotiations are recognized as a means of attaining reciprocity for a certain share of the trade. As to the degree of its specification, the formula follows the Kennedy Round approach which relied mainly on across-the-board concessions and only exceptionally on more specific negotiations. The global character of the Polish formula is also in conformity with the solution adopted in the Havana Charter for the state monopolies.

The Polish reciprocity arrangement, however, suffers from some important weaknesses. First of all, the formula does not pay enough attention to the balance-of-trade criterion of reciprocity. It does not establish any direct link between export and import performance to the disadvantage of Poland which suffers from permanent balance-of-payment pressure. Secondly, the Polish import commitment is to be evaluated on the basis of current dollar prices. No inflation clause or provision permitting adjustments for the fall of the dollar *vis-à-vis* other currencies are included in the Polish-GATT arrangement. This is a serious omission which also works to the disadvantage of Poland's GATT partners and may considerably limit the effectiveness of Polish concessions. Finally, the global character of the Polish commitment, and especially the lack of explicit recommendations for negotiation on specific import targets, did not seem an appropriate framework in which to determine Western market openings for Polish exports. This point will be elaborated upon in Chapter 6.

Poland's 7 per cent annual commitment was replaced three years later by a compound commitment. It provided essentially for the same average rate of import increase per annum, but it was to be calculated over a longer range of time.¹⁰ This rendered the Polish cooperation with the GATT much more flexible – since a shortfall of Poland's imports in one year could be offset by a satisfactory import performance in another year and an average of 7 per cent import increase could be maintained.

In spite of its serious weakness, the Polish reciprocity formula is still important, for it provides an example and has subsequent influence on negotiations with other state-trading countries acceding to the GATT.

ROMANIAN RECIPROCITY FORMULA

Though at the time of its accession to the GATT, Romania – like Poland – was a target-protected economy, it decidedly opposed any type of arrangement based on an obligation to increase imports from the GATT countries.

Romania was a low-income economy. It was thought that this should be kept in mind in negotiations on the reciprocity formula with GATT

members. The GATT should not expect the less-developed countries to make contributions that were inconsistent with their development needs.

The main Romanian criticism of the Polish reciprocity arrangement concerned the lack of a direct link between exports and imports. Romania, suffering from a chronic trade deficit, considered that a reciprocity formula of the Polish type would be contrary to its balance-of-payments interests.

The Romanians proposed instead an arrangement strongly emphasizing the balance-of-trade aspect of reciprocity. They suggested that Romania's earnings from exports to the GATT countries could be fully spent on imports from the GATT area.¹¹ In other words, the proposal suggested balancing both the incremental and the existing trade flows between Romania and its GATT partners as a standard of reciprocity.

The final text of the arrangement provided that, in exchange for better access to the GATT markets, Romania firmly intends:

to increase its imports from the contracting parties as a whole at a rate not smaller than the growth of total Romanian imports provided for in its Five-Year Plan.¹²

The expression 'firmly intends' implies that it is much more a declaration of Romania's intention than a firm commitment as, for example, those included in the GATT schedules of concessions. In that respect the Romanian arrangement is consistent with her claim to developing country status.

Moreover, the arrangement does not refer to any specific rate of import increase as was the case for Poland. Whereas Poland undertook to increase its imports from GATT countries at a rate mutually agreed to in advance, Romanian planners were to fix the rate themselves. Nor did the Romanian solution provide explicitly for target negotiations. Nevertheless, such negotiations, based for instance on an item-by-item approach, could probably be conducted when desired under Article XVII:3 of GATT, against which Romania presented no reservations.¹³

The Romanian arrangement also distinguishes between imports from the contracting parties and total Romanian imports. It seems to aim at assuring the GATT countries of, what could be called, a 'fair share' of total Romanian imports. From the economic perspective the 'fair share' approach is not fully understandable in the context of GATT principles. It is hardly possible to relate it to the GATT concept of non-discrimination or to the provisions on regional integration. 'Fair share' in import expansion says nothing about non-discrimination, or protection – and non-discrimination and protection are what the GATT is about.

The Romanian promise not to decrease the GATT share of imports in total Romanian imports, however, could be considered the most important declaration of the Romanian party in the GATT. In commercial terms it seems quite straightforward, but in political terms it testifies to Romania's scepticism concerning the future of East European integration and expresses the desire to bolster economic independence *vis-à-vis* the Soviet Union and other non-GATT CMEA countries.

HUNGARIAN RECIPROCITY FORMULA

Hungary considered its customs tariffs a main protective element and desired to accede to the GATT on this basis. Therefore, the function and effects of the Hungarian tariffs and the applicability of the GATT traditional reciprocity formula became the main objects of examination during negotiations with Hungary.

The Hungarian tariff approach met with scepticism from some GATT countries (especially the European Community members, Canada, the United Kingdom and Sweden). They noted that the effectiveness of the Hungarian tariff could be weakened by quotas, operation of monopolies on the domestic markets and restrictions on free price formation in Hungary. It was thus put forward that a quantitative import commitment along the lines of the Polish solution was required to assure reciprocity at least during an initial period. If the Hungarian tariff proved effective, a quantitative commitment would then be replaced by a tariff arrangement.

The Hungarian Government contended on its part that it did not dispose of any direct means to guarantee the value of overall imports from the GATT countries, since no import targets were maintained for trade with the market economies.¹⁴ Besides, it noted that most GATT countries combined tariffs with other instruments of trade control and that this did not prevent them from agreeing on the exchange of tariff concessions.

A final decision on the matter was postponed to the last moment. Some delegations preferred to assess the role and functioning of trade control in Hungary before accepting tariffs as an instrument of Hungarian concession-making. Others waited till after the negotiation of the Hungarian tariff schedule in order to see what increase of exports to Hungary could result from Hungary's concessions.

Recognition of the Hungarian tariffs as an effective instrument had a significance far beyond technical considerations. The political dimensions of the issue certainly had an important impact on the final decision of the Western governments.¹⁵

Hungary negotiated its schedule of tariff concessions with GATT members on the basis of the revised but relatively high level of Hungarian tariffs. This high level of tariffs was explained by the fact that

during the transition from central pricing to a market price system, the equilibrium of the economy required protection.¹⁶ No reasons were given as to why this could not be accomplished by a devaluation of the Hungarian currency.

Tariff reduction was the only commitment the Hungarian Government undertook in its schedule. No obligation to increase imports from the GATT territories at a fixed rate, nor to increase those imports at a rate roughly equivalent to the growth of total imports, was included in the Hungarian schedule. There was only the stated intention on Hungary's part 'to increase its imports from contracting parties'.¹⁷

Thus the GATT countries accepted the tariff approach as valid for Hungary and concurred that reciprocity could be reached on the basis of a symmetric reciprocity formula as traditionally adopted in the negotiations of tariff-protected members of the GATT. In this respect Hungary followed the Yugoslav example of participation in the General Agreement.

NON-DISCRIMINATION

ACCESS TO THE WESTERN MARKETS

By virtue of their accession to the GATT, Hungary, Poland and Romania obtained or confirmed the already existing MFN treatment in respect of tariffs in the overwhelming majority of the GATT countries. Neither Hungary nor Romania, however, obtained MFN status in the United States upon entering the GATT. Securing MFN treatment in the United States was an important objective of the Romanian and Hungarian policy-makers. It would certainly have boosted the export of certain food products, textiles and handicrafts across the Atlantic, since the difference between the United States' MFN tariff rate and its normal rate in this range of goods is quite substantial.¹⁸

The fact that the United States, departing from its treatment of Poland and Yugoslavia, refused MFN status to Hungary and Romania considerably limited the advantages they derived from participation in the GATT. However, the accession to the GATT of Hungary and Romania certainly created a more favourable climate for the conclusion of MFN trade agreements with the United States at some further date.¹⁹

The important policy clashes concerning discrimination against Poland, Romania and Hungary resulted from the discriminatory quantitative restrictions maintained by some West European countries (mainly the European Community countries, the United Kingdom, Sweden, Finland and Austria).²⁰ The negotiations, aimed at the global elimination of QRs, were a fiasco.

Hungary, Poland and Romania considered that the discriminatory QRs should be eliminated immediately, since they were contrary to Article XIII of the GATT. The following arguments were set forth in support of this requirement. First, it was pointed out that the elimination of discriminatory QRs on Hungarian, Polish and Romanian exports in the West was the main motive underlying the three countries' interest in accession to the General Agreement.²¹ Thus Western refusal to eliminate the discriminatory QRs could considerably reinforce political opponents of accession in these countries. Secondly, maintenance of the discriminatory restrictions was prejudicial, not only to the East European economies, but also to other GATT countries which did not maintain discriminatory QRs on East European exports.²² Thirdly, maintenance of the restrictions conflicted with the desire of some GATT members (the United States, Canada and Australia) to preserve the 'clarity', of the GATT rules. Moreover, if maintained, the discriminatory restrictions could become the object of bilateral negotiations between East Europeans and some Western governments. This in turn could lead to conclusion of bilateral arrangements, conflicting with the objectives of the GATT.

Governments with discriminatory QRs on Hungarian, Polish and Romanian exports argued that their existence stemmed from historical circumstances and that the economic consequences of their sudden removal were too great to allow such action. Instead, it was suggested that the QRs be eliminated gradually during a transitional period to be agreed upon.²³

The final solution of the problem, as included in the Polish, Romanian and Hungarian protocol for accession, provided that there was to be no increase in the discriminatory aspect of the QRs on East European exports. In fact, the restrictions were to be progressively reduced and wholly eliminated at the end of a transitional period. If, for exceptional reasons, any discriminatory restrictions or prohibitions were still in force, they should be subjected to the scrutiny of the GATT and eliminated as soon as possible. During the negotiations, Poland refused to agree on the above escape clause, so no termination date for the transitional period was established at the time of Poland's accession.²⁴ Hungary and Romania, which accepted the above-mentioned escape clause, agreed that the transitional period would end on 1 January 1975. Due to the vagueness of the Polish arrangement, the fixing of the final date dragged on for years and it still has not been set.

The desire of the East European newcomers to eliminate Western discrimination against their exports in the GATT, therefore, met with only partial satisfaction. It was hoped, however, that participation in the GATT could provide an opportunity for an early solution of the problem.

ACCESS TO THE EAST EUROPEAN MARKETS

Hungary, Poland and Romania claimed that operation of their foreign trade enterprises (state-trading enterprises) was non-discriminatory in the GATT sense. There was however, some divergence of views as to the applicability of Article XVII of the GATT to their state-trading systems.

For reasons that were not very precisely expressed, Poland maintained that state trading, in the sense of Article XVII of the GATT, did not exist in Poland, nor did any import monopoly in the sense of Articles II:4 and XVII:4 (b). Poland held that its foreign trade units were guided by commercial considerations in conformity with the requirements of the relevant provisions of the GATT. On these grounds it refused to provide notification in accordance with Article XVII, while agreeing that the issue of non-discriminatory operation of Polish foreign trade units could be examined during periodic and *ad hoc* consultations.²⁵

Whether Article XVII is applicable to state-trading units operating in the political and economic systems of the CMEA countries was questioned again in the case of Hungary. Originally, Hungary was willing to present reservations to Article XVII:3. The following reasons were set forth:

Hungarian enterprises cannot be considered as obstacles to the expansion of international trade, since by the very nature of their task they work for the expansion of this trade.²⁶

Although the question was valid, as to whether the GATT attitude towards state trading (as manifested in Article XVII) was an appropriate one for the state-trading systems, the Hungarian argument has to be considered as either a sophism or a misunderstanding of the problem. Finally, Hungary did not present any reservation to Article XVII. In addition, Hungary held that no import monopolies in the sense of Articles II:4 and XVII:4 of the GATT operated in Hungary. The latter declaration had to meet with scepticism in light of Hungarian foreign trade practice (see Chapter 4). The attitude of Poland, and the initial objection of Hungary, were in contradiction with the attitude accepted by Romania. Romania accepted Article XVII without any objection and agreed to provide the required notifications on state trading.²⁷

The problem of the applicability of GATT Article XVII to the state-trading systems however, was of little practical importance. There was always a possibility under the protocol for accession to review the operation of state-trading enterprises on request or during the periodic consultations.

Negotiations with Hungary, Poland and Romania were also concerned with the non-discriminatory character of direct trade control and the state-trading link. Poland and Romania held that limitations put on

import levels by restrictive plan targets did not exceed those justified under Article XII for balance-of-payments reasons.²⁸ Both countries declared their readiness to apply those restrictions in a non-discriminatory manner: however, neither the Polish nor the Romanian protocol, provided for more specific rules on the non-discriminatory operation of state-trading than those already included in the GATT. Nor could the information requirement pertaining to targets be brought into line with that referring to quotas under Article XIII:3 (a). Poland and Romania maintained that any obligation to report on specific positions of their foreign trade plans (plan targets) would be contrary to the commercial interests of their foreign trade units.²⁹

Supervision of the non-discriminatory operation of target control was left entirely to the periodic consultation procedure. But the matter was not of great practical importance since Polish and Romanian targets for trade with the market economies were not country-specific. However, there was some need for concern as to the non-discriminatory operation of East European licensing systems. In all three countries individual licences were maintained on at least part of foreign trade; so governments could differentiate among countries or groups of countries in order, for example, to fulfil bilateral agreements. Indeed, some bilateral agreements concluded by Hungary with certain GATT countries required that both partners issue import licences up to the value of the negotiated quota. Hungary argued that these quotas represented an inter-state fixing of contracts previously concluded by enterprises on commercial criteria.³⁰ In her opinion to agree in advance to issue licences for import transactions concluded in a non-discriminatory manner did not indicate discrimination in the licensing systems.³¹ Some delegations, however, felt that in view of Hungary's individual licensing system the geographical distribution of her imports would warrant regular scrutiny. This was to be carried out in periodic consultations with the Hungarian authorities.³² A similar approach was accepted for Poland and Romania.

The restrictive character of the licensing was important in the context of Hungary's claim that tariffs constitute an essential instrument of trade control. According to Hungary the only quantitative restrictions operative in the licensing system were quotas. It was held that in the past years more import licences were issued than were actually used by Hungarian enterprises.³³ This argument, however, was not sufficient proof that the system's restrictiveness did not surpass the limits imposed by quotas.

Hungary justified the maintenance of quotas by balance-of-payments considerations and agreed to consult under the relevant articles of the GATT.³⁴

When acceding to the GATT, Hungary, Poland and Romania expressed their dissatisfaction with bilateralism in trade with the same

developing countries who were members of the GATT. But at the same time the three countries recognized that where trade liberalization was not possible on a non-discriminatory basis it might be better to ensure the expansion of trade through bilateral commitments than to make no progress at all.

Hungary, Poland and Romania pointed out that they were not alone responsible for bilateral trading with some GATT member countries and noted that removal of bilateralism depended strongly on whether these countries desired such a move.³⁵

They noted, as well, that a particularly disturbing feature was a persisting tendency among some developed market economies to favour bilateralism in their relations with Eastern Europe.³⁶

There were doubts about the non-discriminatory operation of the Hungarian tariff system in view of the tariff exceptions written into cooperation agreements between Hungary and several neighbouring market economies. The compatibility of these agreements with the MFN clause was examined by the GATT.³⁷ The conclusion reached may be said to give effective support to non-discrimination while nominally abandoning it: the unconditional form of tariff concession was restricted to only certain beneficiaries. The question had already arisen with regard to Canadian tariff reductions on automotive products. Canada made a *de facto* differentiation between countries whose automobile industries manufactured in Canada (for example, the United States) and those that did not, but no formal violation of the MFN rule had been denounced by the Contracting Parties.³⁸

In the case of Hungary, a similar distinction was introduced between products originating in countries with which Hungary had signed industrial cooperation agreements and other countries.

Upon entering the GATT, Hungary, Poland and Romania did not consider the possibility of joining the IMF, nor were they willing to enter into special exchange agreements with GATT countries.³⁹ The Contracting Parties agreed to release Hungary, Poland and Romania from this latter obligation. The three countries promised instead to act in a manner fully consistent with the principles of the special exchange agreement.⁴⁰ Thus the solution adopted for Hungary, Poland and Romania followed the lines of the arrangement with Czechoslovakia and non-IMF market economies.

When acceding to the GATT, Poland and Romania maintained that export subsidies, as described under Article XVI, had no function in their economies.⁴¹ Hungary declared that its subsidies operated in conformity with the GATT. It justified the maintenance of subsidies on the following grounds: first, they were made necessary by the average features of the exchange rate, which went against some export products.⁴² Secondly, subsidization of exports in other countries obliged Hungary to do the same in order not to leave competing Hungarian

products at a disadvantage on the world market. Thirdly, balance-of-payments and full employment policies justified subsidization of certain exporting enterprises which were not efficient enough to compete on the world market.⁴³ Subsidies were not supposed to lead to dumping but rather to eliminate the difference between domestic and foreign prices. These arguments are not wholly convincing. The granting of subsidies to about two-thirds of Hungarian exporting enterprises would seem primarily due to the overvalued forint.⁴⁴ The balance-of-payments justification of subsidies seems quite irrelevant in the GATT context, which offers other means to attain this end. The Hungarian export subsidies could be considered, however, to be compatible with the GATT, and Hungary agreed to respect the relevant GATT obligations.⁴⁵ In bringing domestic price formation into conformity with the GATT, a double standard was applied — one treatment was given to Poland and Romania and another to Hungary. Poland and Romania considered that when they fixed domestic prices, the interests of exporting countries were adequately accounted for and prejudicial effects avoided.⁴⁶ Although they refused to give any assurance as to the level of domestic prices for imports they promised that these prices would naturally be fixed at levels permitting the sale of goods. There was obviously no interest in importing goods merely to augment stocks.⁴⁷ Taking into consideration the target control of foreign trade, price formation in Poland and Romania was recognized as being without prejudice to partner countries. In the case of Hungary, which claimed tariff protection *vis-à-vis* the market economies, the existence of fixed prices might provide additional protection for domestic producers. Therefore, the issue was of particular concern. After due examination it was concluded that the Hungarian price system was free in a:

sufficiently wide sphere to make it possible that in general the customs duty should definitely influence the price formation.⁴⁸

Thus there appeared to be no incompatibility between the Hungarian price system and Article III:9 of the GATT in this connection.

In general, the behaviour of the Hungarian, Polish and Romanian foreign trade systems *vis-à-vis* members of the GATT was recognized as mainly non-discriminatory and in accord with the respective requirements of the General Agreement. It was, however, noted that some special supervisory procedure could be required in order to provide a guarantee for the future. One of the important omissions of the Polish and Romanian protocols for accession seems to be the lack of specific rules on the non-discriminatory operation of plan targets. Plan targets constituted the main protective element in both countries and the GATT failed to provide a code of non-discrimination for these economies. Nor

was the information requirement pertaining to targets brought in line with that dealing with quotas or licensing.⁴⁹

INTRA-CMEA TRADE AND NON-DISCRIMINATION

There were two possible ways of approaching the problem of intra-CMEA trade in the context of non-discrimination. The relations of Hungary, Poland and Romania with the centrally-planned economies (especially with the CMEA members) could be considered an exception to the general MFN treatment on the grounds of regional integration (Article XXIV). There was, however, no place for planned regional integration under Article XXIV; the article in question would either have to be modified or a waiver granted. A second approach would be to affirm that the difference in the trading methods of the centrally-planned economies would not saddle the market economies with any new disadvantages; these methods did not necessarily mean discrimination against the West. The GATT countries opted for the second approach.

The question was discussed only marginally in the case of Poland and Romania, which used targets both for trade with the market economies and trade with the centrally-planned economies. Both countries maintained that, although the payments advantage might be incidental in their trade with the centrally-planned economies, there were more basic reasons why these countries should continue to be more important trading partners than the Western economies; the proximity of the centrally-planned economies; and the long-standing character of their economic relations and cooperative action in fields other than commerce were mentioned.⁴⁹ Poland, Romania and Hungary argued that there was no *de facto* discrimination in favour of the CMEA members in their foreign trade.

For both political and technical reasons it was difficult for the Western members of the GATT to uphold the contrary view. Politically, the special economic links of Poland, Romania and Hungary with other CMEA countries were not negotiable.⁵⁰ They could thus either be recognized as discriminatory in which case the CMEA must be accepted as a regional arrangement under the GATT, or the matter could be passed over in silence and intra-CMEA trade considered in formal accord with the non-discriminatory provisions of the GATT.

Recognizing intra-CMEA trade relations as regional trading was certainly not in the interest of the GATT countries; it would mean confirming the intra-CMEA economic relations and that was neither politically nor economically desirable in the West. Besides, checking on discrimination between the two areas in Hungarian, Polish and Romanian foreign trade through comparisons of respective price levels would not be practicable. First of all, intra-CMEA trade is highly

bilateral, engendering a proliferation of multiple fraction markets within CMEA itself. Secondly, CMEA prices are often irrational and unbalanced. Thirdly, as there is no explicit equilibrium exchange rate between Western convertible currency and the rouble it is difficult to compare world prices with CMEA prices. Finally, any supervision of 'non-discrimination' based on comparison of the protective elements employed by Poland, Romania and Hungary must constantly evaluate and compare the targets for trade with the centrally-planned economies and the targets (Poland and Romania) and tariffs (Hungary) for trade with the market economies. Both methods are too complex to be practicable under the GATT.

Further discussion on whether CMEA countries were discriminated against under the Polish, Romanian and Hungarian trade systems thus appeared rather theoretical. Certainly, the view was widespread among Western governments that the Western share in Hungarian, Polish and Romanian trade was relatively low, due, *inter alia*, to anti-West discrimination. Nevertheless the pragmatically-minded negotiators preferred to abandon a largely abstract discussion of discrimination and deal with the means of obtaining what could be referred to as a 'fair share' in the expansion of Polish, Romanian and Hungarian imports from GATT and non-GATT areas.

Though the Polish protocol did not spell out any standards of fairness for the increase of imports from the GATT area, it did provide for a supervision of Polish trade developments which could be considered relevant to the issue. It was up to the consultation forum to judge whether the

development of Polish imports of various categories of goods (for example agricultural goods, raw materials, semi-manufactured goods, machinery and consumer goods) from the territories of contracting parties in relation to development of Polish imports from other countries

respected the spirit of the GATT.⁵¹ The 'fair share' approach was adopted in the case of Romania and could be considered as one of the main Romanian concessions under the General Agreement.

Trade relations with centrally-planned economies were explicitly mentioned for the first time, in the Hungarian protocol.⁵² The protocol provided that Hungary should not be prevented from maintaining existing regulations for trade with centrally-planned economies. Nevertheless, at the same time, Hungary promised that these regulations should not impair her commitments, discriminate against or otherwise operate to the detriment of contracting parties.⁵³

During the consultations, special attention was to be accorded to the

Hungarian regulations for trade with the centrally planned economies.⁵⁴

In conclusion, the special links between Poland and Romania and their CMEA partners were not directly dealt with in the respective protocols for accession. Provisions were introduced, however, permitting supervision of the 'fairness' of expansion of Polish and Romanian imports from GATT countries. In the case of Romania, the standard of fair expansion by means of a comparison between imports from the two areas was introduced.

Only the Hungarian protocol explicitly referred to the problem of special relations between Hungary and the centrally-planned economies. The protocol recognized the existence of these relations, while providing that they should not detrimentally affect the interests of other GATT members.

ESCAPE CLAUSE AND CONSULTATION

DUMPING AND SAFEGUARD CLAUSE

The provisions of the GATT concerned with dumping could prove unworkable in the case of a target-protected and fixed-price economy. It was thus necessary to modify the respective provisions as they would be applied to Romania and Poland. This modification consisted of two definitions of the 'normal value' of the product as set down in Article VI: either the price that generally prevailed in the market of the importing GATT countries or, if the first definition was inapplicable, the product value based on the price of a similar product originating in a third country.⁵⁵ The solution adopted for Poland and Romania followed the standard of dumping as already practised in relations between the GATT countries and Czechoslovakia.

Given the above definition of 'normal value', Article VI became practicable for the target-protected economies. Poland and Romania agreed to consult whenever there were allegations that the prices of their products were considerably lower than prices quoted by other suppliers.⁵⁶

It is noteworthy that although Hungary maintained a price system that was considered 'sufficiently' free and used tariffs to trade with the market economies, the definition of 'normal value' used for Poland and Romania was also adopted for Hungary. There were doubtless practical reasons for this, as well as a certain lack of confidence in the functioning of the Hungarian 'new economic mechanism' among the GATT countries. The solution adopted has the advantage of being simple and relatively clear in application. But where Hungary, Poland or Romania were the most efficient producers of a given product, it would have to reduce the competitive situation and adjust the export price to the level

of the most efficient producer elsewhere. From a practical point of view, however, this would not be likely to result in a substantial deviation of trade.

The safeguard clause, providing for release from GATT obligations when growth of imports exceeds the adjustment capacities of the domestic producer turned out to be of particular importance in relations with state-trading economies. Many Western governments believed that to permit the dynamic development of East-West trade and to cope with certain peculiarities of the East European foreign trade systems, some sort of special protective mechanism against market disruption was necessary. Since Articles XIX and VI of the GATT already dealt with this matter, it is interesting to compare them with the specific arrangements adopted for Poland, Romania and Hungary.

The special escape clause included in the Hungarian, Polish and Romanian protocol differed considerably from Article XIX. Under Article XIX use of the escape clause must be based on MFN treatment. Obligations under the GATT are suspended or concessions are withdrawn *vis-à-vis* all exporters of a given product, whereas under the protocol the escape clause may be invoked against an individual country, even when this country is not the only exporter on the market. In the case of Poland, the safeguard clause is not reciprocal – while GATT countries are free to use it against Poland, this country is not free to do the reverse.

The specific clauses may have important disadvantages for Hungary, Poland and Romania. As the only countries subject to this special escape clause, these countries may find it difficult to lift import restraints or negotiate compensatory remedies, for the simple reason that they have fewer means of retaliation than a group of countries hurt by withdrawal of concessions under Article XIX of the GATT. What is more, illegal quantitative restrictions on Hungarian, Polish and Romanian exports may be replaced by legal restrictions under the escape clause. This will in no way improve the access of Hungarian, Polish and Romanian agricultural products to the European Community market and other West European countries.

Hungary, Poland and Romania, however, also recognized the Article XIX safeguard clause. In Poland's case, should the value of imports from the GATT territories fall demonstrably short of the agreed figure, the situation would be dealt with under procedures analogous to the nullification and impairment provisions of Article XXIII.⁵⁷

In sum, the GATT dumping provisions were adopted for relations with Hungary, Poland and Romania by redefining the 'normal value' as set down in article VI of the GATT. The 'normal value' of goods is determined in reference to external prices rather than to the domestic prices of state-trading countries. A reinforced safeguard mechanism is devised for relations with the three countries abandoning the non-

discrimination principle when action was undertaken against goods exported by the East European members of the GATT.

CONSULTATIONS AND INFORMATION

The arrangements made for Hungary, Poland and Romania in the GATT relied largely on periodic consultations with the contracting parties. Consultations were expected to provide a multilateral forum for controlling the operation of the respective protocols and supervision of new developments in East-West trade relationships under the GATT. The periodic consultations were particularly concerned with two aspects regulated by the protocols of accession: (i) the elimination of discriminatory quantitative restrictions maintained by some members of the GATT on Hungarian, Polish and Romanian exports; and, (ii) development of Hungarian, Polish and Romanian trade in various categories of goods, especially the general trend in geographical distribution of that trade. Supervision of the geographical development of trade was expected to reinforce the GATT's required 'fair share' of expanding East European imports. For Hungary, the consultations explicitly concerned the Hungarian trade development with the centrally-planned economies and specifically those aspects of that trade which might constitute a potential danger of discrimination against members countries of the GATT.

In sum, periodic consultations with the three countries were meant to control those conflicts in East-West trade which went partially unresolved under the respective membership arrangements.

Apart from the annual consultations (Poland) and biennial consultations (Romania and Hungary) there also existed the possibility for *ad hoc* consultations upon the request of any GATT country party to the arrangements.⁵⁸

The GATT's supervisory role in the development of East-West trade required access to the appropriate information. Since the lack of such information had been, for years, a serious obstacle to the development of East-West trade, the GATT signatories asked Hungary, Poland and Romania to provide more adequate information on foreign trade legislation and statistics.

The three countries promised to provide the required data in conformity with the GATT's Article X. Hungary and Romania also agreed to use the GATT questionnaire on state trading. Poland considered this notification scheme inappropriate and offered instead to supply necessary information preceding periodic consultations.⁵⁹ A special reporting scheme was arranged for periodic consultations with Hungary, Poland and Romania. Poland and Romania refused, however, to report their import targets in advance because of the unfavourable effect this could have on the prices of imported goods. Romania

declared that when advance information on certain targets was needed it could be furnished on an *ad hoc* basis.⁶⁰

SUMMARY AND CONCLUSIONS

The three arrangements attempted to render the terms of Polish, Romanian and Hungarian membership in the General Agreement comparable with those of other member countries. For Poland and Romania they provided a reciprocity formula based on the exchange of tariff concessions against import commitments. Poland agreed to expand its imports from the GATT area globally by 7 per cent a year. Romania, claiming to be a developing country, was allowed entrance to the GATT under a reciprocity arrangement which stipulated that Romanian imports from the GATT countries should increase at a rate no smaller than planned for total Romanian imports.

The weaknesses of the Polish commitment were:

- (a) the lack of a direct link between the Polish import and export performance;
- (b) the failure to specify groups of commodities for which Poland might grant particularly interesting concessions to; and,
- (c) the omission of the inflation clause in the 7 per cent import undertaking.

The first two points, as will be shown later on, proved to be of particular disadvantage to Poland. The last one could considerably limit the benefits of Polish membership for its GATT partners.

The 'liberal' characteristics of its system of trade with the West permitted Hungary to claim tariff as the effective instrument of trade control and to declare its internal markets 'sufficiently' competitive. The Hungarian symmetric reciprocity formula is an interesting one and may provide a pattern for other state-trading systems willing to introduce effective tariff protection. To that extent, Hungary followed the Yugoslav approach in the General Agreement.

The GATT was not very successful in providing a mechanism for assuring non-discrimination in East-West trade. It did not bring the West European countries to immediate elimination of their discriminatory quantitative restrictions on East European exports. It did not provide any satisfactory standards for non-discriminatory operation of foreign trade plan targets in Poland and Romania. Finally, and this point is the most important, the GATT acted as though there were no problems of CMEA integration. Instead of setting the matter on the basis of non-discrimination, it opted for a pragmatic and rather implicit solution based on a requirement of 'fair' import expansion. This

approach says nothing about protection; and protection is what the GATT is expected to be about.

The 'fair' expansion of Polish, Romanian and Hungarian imports was to be tested through scrutiny of the geographical development of their imports during periodic consultations. Only in the case of Romania were the criteria of 'fair' import expansion spelled out. They provided that the rate of growth of Romanian imports from GATT countries should not be inferior to that from non-GATT countries (including Romania's most important CMEA partners). That provision may be looked upon as the most important political concession made by Romania under the General Agreement.

In sum, the GATT's pragmatism was thus particularly apparent in its approach to the question of non-discrimination in East-West trade, which was, to a large extent, left to consultation forums.

Finally, the GATT's dumping provisions and safeguard mechanism were modified to suit the conditions of East-West trade and to soothe the West's fears concerning the unfair practices of East European exporters.

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2. C. H. von Platen, 'Problems and Possibilities of East-West European Trade', *Skandinaviska Banken Quarterly Review*, Stockholm, July 1958, pp. 79-84.
3. Jacques A. L'Huillier, 'Problèmes relatifs au développement des échanges entre les économies de libre entreprise et les économies collectivistes', study prepared for the International Chamber of Commerce, Paris, April 1960 (Doc. 102/1).
4. Eric Wyndham White, 'Looking Outwards', address to the General Export Association of Sweden, Stockholm, April 1960.
5. *The Work of the Economic Commission for Europe on Trade and Development*, E/CONF. 46/PC/47 (Geneva: December 1963) p. 10.
6. GATT Doc. TN. 64/NTB/1, October 1963, p. 3.
7. GATT Doc. TN. 64/NTB/9, November 1964, p. 2.
8. GATT *Basic Instruments*, 15th Supplement, 1968, p. 52.
9. *Ibid.*, p. 52.
10. GATT *Basic Instruments*, 18th Supplement, 1972, p. 201.
11. GATT Doc. Spec. (69) 86, June 1969, p. 3.
12. GATT *Basic Instruments*, 18th Supplement, 1972, p. 10.
13. During the negotiations with both Poland and Romania the matter of granting concessions on single commodity targets was briefly touched upon. In both cases the East Europeans argued that a product-specific import commitment could have detrimental effects on their import interests.
14. GATT Doc. Spec. (71) 1, January 1971, p. 5.

15. As noted in Chapter 1, many Western GATT members supported the efforts of East European governments towards economic decentralization. Certainly, the Hungarian tariff approach in the GATT was a direct result of the economic reform in Hungary (the so-called 'new economic mechanism'), which had to overcome many domestic and external political and ideological restraints before being accepted. Recognizing the Hungarian tariff as an instrument of participation in the GATT could thus appear politically desirable in the West.
16. GATT Doc. Spec. (70) 83, September 1970, pp. 9–15.
17. GATT Doc. Spec. (72) 83, August 1972, p. 5; and *Basic GATT Instruments*, 20th Supplement, 1974, pp. 37–41.
18. The importance, however, of MFN status for Hungary and Romania on the American market can be overstated. The granting of MFN treatment to Poland by the United States did not result in an important increase in the Polish share of the American market, primarily because of the badly organized distribution system of Polish exports in the United States and the existence of numerous non-tariff barriers on agricultural products. The similarities to be drawn between Polish exports to the United States and those from Hungary and Romania indicate that American MFN treatment would have had a limited impact on the expansion of Hungarian and Romanian exports. See Thomas A. Wolf, 'Effects of U.S. Granting of Most Favored Nation Treatment to Imports from Eastern Europe: The Polish Experience', Reprint Series of the International Institute of Management, Berlin, 1973, p. 22.
19. Romania obtained MFN treatment in the United States at the end of 1974. It is not certain, however, whether the clause will be maintained in the future.
20. By discriminatory restrictions are meant QRs that are contrary to provisions of Article XIII of the GATT.
21. As an indication of the economic importance of the issue: Hungary, for example, estimated that West European discrimination (discriminatory QRs) and United States' discrimination (lack of MFN treatment on the United States market), resulted in an annual loss to the Hungarian economy of \$20–50m or about 6–15 per cent of the value of Hungarian exports to the developed market economies. See *Polityka*, Warsaw, March 1974, no. 9 (887), p. 13.
22. Countries like the United States, Japan, Canada and Australia, which did not maintain any discriminatory restrictions on East European exports, strongly supported the Polish, Hungarian and Romanian requirement for immediate elimination of QRs.
23. The European Community governments let it be known that if Poland, Romania and Hungary insisted on immediate removal of the discriminatory QRs they would be forced to invoke Article XXXV of the GATT. This would deprive the East European countries' presence in the GATT of any practical importance.
24. It was expected that the end of the transitional period could be fixed during the course of the third annual consultations with Poland. See *GATT Basic Instruments*, 15th Supplement, 1968, p. 48.
25. GATT Doc. L/3653, Add. 11, June 1972, p. 3.
26. GATT Doc. L/3426, September 1970, p. 26.
27. GATT Doc. L/3653, Add. 10, June 1972, p. 2.
28. GATT Doc. L/3211, May 1969, p. 16 and GATT Doc. MFT/81/58, Add. 1, October 1958, p. 8.

29. GATT Doc. Spec. (69) 110, September 1969, p. 15.
30. GATT Doc. L/3426, September 1970, p. 16.
31. *Ibid.*, pp. 15–16.
32. GATT *Basic Instruments*, 20th Supplement, 1974, p. 8.
33. GATT Doc. L/3426, September 1970, p. 16.
34. *Ibid.*, p. 16 and GATT *Basic Instruments*, 20th Supplement, 1974, pp. 37–41.
35. See Chapter 6.
36. GATT Doc. L 1037, Add. 1, September 1959, p. 2, GATT Doc. L 3211, May 1969, p. 14. GATT Doc. L/3426, September 1970, p. 5.
37. The Secretariat was asked for a legal opinion in the matter.
38. GATT Doc. L/2409, March 1965.
39. Romania became a member of the IMF in 1972 after her accession to the GATT.
40. See paragraph 8 of the Polish, Romanian and Hungarian protocols for accession.
41. GATT Doc. MGT/81/58, Add. I, October 1958, p. 11; GATT Doc. L/3211, May 1969, p. 18.
42. GATT Doc. L/3301, January 1970, p. 14.
43. GATT Doc. L/3426, September 1970, p. 25.
44. Balassa, 'Der Neue Wirtschaftsmechanismus in Ungarn', in Hans-H. Höhmann, Michael Kaser, Karl Thalheim (eds), *Die Wirtschaftsordnung Osteuropas im Wandel* (Freiburg: Verlag Rombach, 1972) vol. 1, p. 203.
45. GATT *Basic Instruments*, 20th Supplement, 1974, p. 7.
46. GATT Doc. L/3211, May 1969, p. 17; GATT Doc. MGT/81/58, Add. 1, October 1958, p. 10.
47. GATT Doc. TN/64/NTB/1, October 1963, p. 4; GATT doc. L 3211, May 1969, p. 17.
48. GATT Doc. L/3301, January 1970, p. 29.
49. GATT *Basic Instruments*, 11th Supplement, 1963, p. 74 and GATT Doc. TN/64/NTB/1, October 1963, p. 2.
50. However, it was admitted by the three East European countries that the share of the CMEA trade in their total trade was not immutable. See GATT Doc. TN/NTB/1, October 1963, p. 3; GATT Doc. Spec. (71) 1, January 1971, p. 2; GATT Doc. L/3301, January 1970, p. 7.
51. GATT *Basic Instrument*, 15th Supplement, 1968, p. 52.
52. Annex B of the protocol enumerates these economies as follows: Albania, Bulgaria, Czechoslovakia, the German Democratic Republic, the Democratic People's Republic of Korea, Mongolia, the People's Republic of China, Poland, Romania, the Soviet Socialist Republic and the Democratic Republic of Vietnam.
53. GATT *Basic Instruments*, 20th Supplement, 1974, p. 4.
54. *Ibid.*, p. 7.
55. Poland and Romania did not join the Anti-dumping Code. Among the other state-trading countries, Czechoslovakia was an original party and Hungary joined the Code in November 1974.
56. GATT Doc. MGT 81 58, Add. 1, October 1958, p. 11; GATT Doc. L 3211, May 1969, p. 19.
57. GATT Doc. TN/64/NTB/15, April 1964, p. 2.
58. Periodic consultations with Romania and Hungary may take place

annually, when requested by any party to the protocol for accession.

59. Poland rightly claimed that the questionnaire did not make sense for state-trading systems, since the list of included products would comprise practically the complete range of imports and exports of a state-trading country. See GATT Doc. L/3633, June 1972, p. 3, and GATT Doc. MGT/81/58 Add. 1, October 1958, p. 12.

60. GATT *Basic Instruments*, 18th Supplement, 1972, p. 6.

GATT Experience with the State-trading Systems

Participation of Poland, Romania and Hungary in the GATT provides a valid lesson of experience in the field of East-West trade co-operation. This chapter starts with the appraisal of the trade concessions exchanged between the East European members of the GATT and other contracting parties. Next, it considers the GATT's role in removal of discrimination and bilateralism in East-West trade. Finally, the issue of reciprocity, as well as consultation and information, is critically discussed.

REDUCTION OF BARRIERS TO TRADE

APPRAISAL OF EAST EUROPEAN CONCESSIONS

Poland has never negotiated its plan targets in the GATT although such negotiations are possible under its formula of reciprocity. Even Poland's global import commitment, calculated in current dollar prices, has been deprived of any real significance – for two main reasons:

- (a) inflation, which increased substantially after Poland's accession; and,
- (b) Reduction in value of the dollar in terms of other Western currencies.

These two factors resulted in a nominal increase in the unit value of Polish imports from the GATT countries (in current dollar prices). Relations between the nominal Polish import commitment and the real import increase required to fulfil that commitment is illustrated in Table 6.1.

The figures in the second column indicate the increase in unit value of Polish imports due both to parity changes and to rise in export prices. Since the Polish import commitment under the GATT was accounted in

TABLE 6.1
Nominal and Real Import Increase Required of Poland under the GATT

	<i>Required nominal per cent increase of Polish imports from GATT area in dollars</i>	<i>Per cent increase in unit value of Polish imports from the GATT area in dollars^a</i>	<i>Real per cent increase in Polish imports from GATT area required under the GATT</i>
1968	7	3	4
1969	7	4	3
1970	7	6	1
1971	7	7	0
1972	7	10	-3
1973	7	11	-4
1974	7	15	-8

^a Estimated on the basis of United Nations Statistical Office data on increase in unit value of exports for area and commodity groups. The average is weighted by the relative importance of commodity groups and areas in Polish imports from the developed market economies. Dollar devaluation taken into account.

current dollar prices, it is evident that a nominal increase of 7 per cent implied a considerably less significant increase in real terms. And from 1970 on, it did not imply any real import increase at all.

Table 6.2 gives data on Polish imports from the countries of the GATT after Poland's accession to the GATT.

A look at the figures shows two distinct periods in the performance of Polish imports from the GATT countries: 1968–70 and 1970–74. Poland's imports from that area increased relatively slowly during its first three years of membership. In 1968 Poland did not fulfil its 7 per cent obligation (Column 1) and in 1969 and 1970 the annual increase of Polish imports from GATT countries only slightly exceeded the contractual 7 per cent nominal increase.

The 1968 shortfall in Poland's import figures can be partly justified on the following grounds: first, since Poland's imports depended on its export capacity, the discriminatory restrictions on Polish exports may have adversely affected the Polish import performance. In 1968 Poland's trade deficit rose from \$17m to \$58m with subsequent repercussions on Polish imports. Secondly, in 1968 Poland's imports from Czechoslovakia – one of its most important trading partners – decreased significantly.¹ Thirdly, many Polish foreign trade enterprises decided to postpone purchases on some markets in the hope of benefiting from the expected devaluations of the French franc and the pound sterling. Since these delays took place in December, Poland's peak import month, the reduction in Polish imports was considerable.² Finally, there was a statistical consideration: the figure indicated by the Central Bank of Poland (8.2 per cent) was calculated on a f.o.b. basis, while the GATT countries' 6.0 per cent figure was on a c.i.f. basis. During 1968 the freight rates had risen significantly.³

The second period of Polish membership (1970–74) was characterized by an extremely important increase in Polish imports from the GATT area. During this period, the annual increase in Poland's imports from the GATT area exceeded the increase of its total imports and that of world imports.⁴ At the same time, imports from GATT countries rose considerably as a percentage of total Polish imports and reached 64 per cent in 1974. These significant import increases coincided with a significant rise in the Polish trade deficit with the West. The deficit increased further by \$400m in 1972 and \$1500m in 1973.⁵

Thus, paradoxically, during the period when Poland's 7 per cent commitment called for a real import increase, the GATT's share in total Polish imports (accounted at constant prices) tended to diminish. On the other hand, Poland's import performance was very satisfactory in a period when the Polish concession under the GATT had become meaningless (1971–74), since it did not guarantee any import increase in real terms. The spectacular increase of Polish imports from the West is to be attributed to the granting of sizeable Western credits to Poland and

TABLE 6.2
Poland's Foreign Trade with GATT Countries and Poland's GNP
(per cent)

Date	Annual increase in imports from GATT countries		Annual increase in total imports		Annual increase in exports to GATT countries	Annual increase in total exports	Annual increase in GNP at constant prices
	nominal ^a	real ^b	nominal ^a	real ^b			
1968	6.0 ^c	3.0	9.0	6.0	7.7	4.9	10.0
1969	9.3	5.7	12.5	8.5	9.7	10.0	3.5
1970	7.9	1.9	12.4	6.4	13.2	12.9	5.7
1971	18.0	11.0	12.2	5.2	12.5	9.2	7.8
1972	48.9	38.9	31.8	21.8	24.5	27.2	10.1
1973	65.3	54.3	43.5	32.5	38.7	30.5	10.0
1974	41.8	37.3	34.2	30.5	40.1	39.9	9.1

SOURCE Calculated from data in GATT documents (Consultations with Poland, Reports).

^a At current dollar prices.

^b At 1967 dollar prices.

^c According to statistics of the Central Bank of Poland, expenditures on imports from GATT countries rose 8.2 per cent in 1968.

was independent of the Polish undertaking in the GATT.

Fulfilment of the Romanian obligation under the GATT could have been measured at the end of the 1971–75 Plan. However, the matter had not yet been examined in the GATT at the time of writing. It may be noted that Romanian imports from the GATT area were increasing at a higher rate than the annual average rate of import growth required to reach the plan objective. Table 6.3 shows the changes in Romanian foreign trade during its membership in the GATT.

The volume target of overall Romanian imports provided for a 61 to 72 per cent rise during the Five-year Plan (1970–75). This implies an average annual trade growth of 11 to 15 per cent. Since the unit value (dollars) of Romanian imports from the GATT area increased at less than 12 per cent for the period 1972–73 and less than 20 per cent for 1974–75, Romanian import performance under the GATT may be termed satisfactory. Romania's membership in the GATT coincided with a particularly dynamic growth of Romania's imports from the developed market economies.

When entering the GATT, Hungary granted tariff concessions on 892 items, or about 50 per cent of the products it imported from the West.⁶ This resulted in a reduction of the average level of MFN tariffs in Hungary by 23 to 30 per cent. The average considerably understates, however, the extent of Hungarian protection. In part import weights were used in the case of prohibitive tariffs, and in part no account was taken of quantitative restrictions and prepayment requirements in Hungary.⁷

It is still too early to evaluate the significance of the Hungarian tariff concessions in terms of trade flows. It may be only pointed out that Hungarian imports of commodities for which tariff concessions were granted rose in 1974 by 63.8 per cent when accounted at current prices. This growth was considerably higher than the increase in imports of items on which no tariff concessions were granted (about 28 per cent) and higher than the increase of global Hungarian imports. Under the concessions, imports from the GATT developed market economies showed the most dynamic growth.⁸ Balance-of-payments difficulties, however, forced Hungary to introduce some restrictive measures against its GATT partners.⁹ These measures considerably limited the significance of the Hungarian tariff concessions granted to GATT countries.

The membership of Poland, Romania and Hungary in the GATT coincided with an extremely dynamic development of these countries' imports from the West. This was brought about, however, through the granting of sizeable Western credits to Hungary, Poland and Romania and not through the East European concessions, which proved either meaningless or of a limited value to GATT countries.

TABLE 6.3
Romanian Foreign Trade with the Countries of the GATT

	Annual percentage increase in imports from GATT countries	Annual percentage increase in total imports	Annual percentage increase in exports to GATT countries	Annual percentage increase in total exports
1971	—	7.3	—	13.5
1972	27.2	24.4	20.8	23.7
1973	26.2	20.0	60.9	29.0
1974	61.2	47.0	44.9	30.0

SOURCE: GATT documents (Consultations with Romania, Reports). Data for 1973 and 1974 based on Romanian national statistics: *Anuarul Statistic Al Republicii Socialiste România, 1974* (Bucarest, 1975) pp. 383-5.

WESTERN CONCESSIONS

Upon their accession to the GATT, Hungary, Poland and Romania acquired direct rights to the tariff concessions previously agreed upon by GATT countries. With all the formal advantages it implied (see Chapter 1) that privilege proved to be of very limited practical importance to East European exporters. First of all, even before their accession to the General Agreement, the three state-trading countries enjoyed *de jure* or *de facto* MFN treatment in almost all GATT countries. Consequently, accession to the General Agreement did not guarantee any important market openings. Secondly, as mentioned earlier, for years Romania and Hungary did not have MFN treatment in the United States in spite of their membership in the GATT. This limited these countries' advantages of participation in the GATT's multilateral trade system. Only recently has the United States Congress made it possible for MFN treatment to be granted to the above-mentioned countries along with the remaining East European countries, non-members of the General Agreement.¹⁰

Another important task which was to have been accomplished 'gradually and progressively' during the Polish, Romanian and Hungarian presence in the GATT was the elimination of the discriminatory quantitative restrictions maintained by some West European countries on the exports from Eastern Europe. The GATT was also largely unsuccessful in fulfilling this task, which was so important for the normalization of trade relations between East and West.

The first important conflict in that respect appeared in relation to the establishment of the final date for elimination of the discriminatory QRs against Poland. Poland claimed that there was a direct link between her obligations *vis-à-vis* the contracting parties and elimination of quantitative restrictions on her exports.¹¹ She underlined that the trade deficit with the developed economies was caused, first and foremost, by the discriminatory quantitative restrictions.¹² The fact that West European quantitative restrictions were indeed burdensome for Polish exporters was made evident by the many cases where relaxation was followed by substantial expansion of Polish exports.¹³ Poland's exports of machinery may be cited as an example. The 37 per cent rise in Polish exports of machinery to GATT markets in 1969-70 was attributed to trade liberalization measures (QRs) undertaken by West European partners.¹⁴

Poland considered that the end of 1974 would be a reasonable time to close the transitional period. Unlike the Romanians and Hungarians, however, the Poles opposed an escape clause that would permit maintenance of some discriminatory restrictions beyond the transitional period. They argued that the partners concerned would have sufficient time (four years) to adjust their economies to the requirement. Poland's

view was shared by GATT countries that did not maintain discriminatory quantitative restrictions against Poland—especially by the United States, Japan and Canada.

The West European governments argued that no direct link between the implementation of Poland's import programme and the establishment of a transitional period could be formally recognized. They noted that the economic circumstances that had led them to establish the discriminatory quantitative restrictions were still in existence. They recognized the necessity to eliminate quantitative restrictions but refused to undertake any firm obligation. Instead, the European Community and a group of other West European economies were ready: 'to remove their quantitative restrictions progressively and to consider it as its objective to eliminate them before the end of 1974'.¹⁵ This proposal did not satisfy the Polish party.

Due to the Community's persistent refusal to agree on a final date of elimination of the discriminatory QRs, Poland brought the question to the attention of the GATT countries first at the Council meeting and later at the Session of the Contracting Parties. However, no solution could be agreed upon.¹⁶

There were two ways in which the discriminatory effects of the quantitative restrictions on Polish, Romanian and Hungarian exports could be removed:

- (a) by abolishing these restrictions, and
- (b) by enlarging the existing quotas.

The Polish experience is a good example for judging the progress in that respect. When Poland acceded to the GATT (1967), the most important Western markets for Polish exports were protected by discriminatory quantitative restrictions. These restrictions usually worked against the products that were Poland's most important exports, for example, live animals and animal products, prepared foodstuffs, textiles, some chemical products and household articles.¹⁷ Even though during the first three years of Poland's membership in the GATT some relaxation of discriminatory restrictions on Polish exports could be noted the progress was very slow.

This is best illustrated by Table 6.4. Though the statistics (second column) are based on Polish estimations (judged too high by some countries concerned), Poland no doubt suffered considerably from the West's discriminatory QRs during its membership of the GATT. The European Community was the object of particularly violent criticism from Poland. The latter claimed that most of the items liberalized by the Community in 1971 and 1972 were goods that Poland did not export at all or only in small quantities.¹⁸ Important relaxation of the discriminatory restrictions by Austria, Denmark, Italy and Sweden from 1971

TABLE 6.4
Discriminatory QRs Against Polish Exports in 1971
(per cent)

<i>Country's imports to the GATT area</i>	<i>Share of country's imports in total Polish exports to the GATT area</i>	<i>Share of Polish exports subject to discriminatory QRs in total Polish exports to the country</i>
West Germany	20.0	40
United Kingdom	15.0	45 ^a
Italy	11.0	15
France	6.0	20
Austria	4.0	15 ^b
Sweden	4.0	30
Benelux	4.0	15
Finland	3.5	15
Denmark	2.5	10
Norway	2.5	5

SOURCE: *Basic Instruments*, 19th Supplement (Geneva: GATT Secretariat, 1973) p. 115; and author's calculations.

^a 15 per cent according to a British statement in the GATT.

^b In volume terms.

on was not so much due to any action from the GATT as to bilateral agreements concluded between each of these countries and Poland. Some doubts may be cast on the compatibility of these agreements with the multilateralism advocated by the GATT. Bilateral agreements, however, still seemed to provide the most efficient method of eliminating the discriminatory restrictions in the West. Following the same approach, the European Community proposed similar bilateral agreements to Hungary and Romania.

The slow elimination of the discriminatory QRs was particularly disquieting in the case of Romania and Hungary, since GATT countries had promised to remove these restrictions by the end of 1974. But, though some QRs were symbolically liberalized at the end of 1974, a large number of hard-core restrictions still continues against Romania and Hungary.

All in all, the GATT forum did not prove very effective in eliminating Western discrimination against Polish, Romanian and Hungarian imports. The matter was of considerable economic importance for some West European industries and Western governments were under constant pressure against removal of the discriminatory restrictions. The East Europeans, on the other hand, disposed of no effective instrument to push their own demands for removal of the discriminatory QRs in the GATT forum.

It is certainly for that reason that the issue was positively solved outside the GATT and on a bilateral basis often in obvious contradiction to GATT principles of multilateralism.

NEW DEVELOPMENTS AND THE GATT PRINCIPLES

NON-DISCRIMINATION AND FAIR IMPORT EXPANSION

The rules of the General Agreement on non-discrimination formally applied also to Hungary's, Poland's and Romania's trade with the centrally-planned economies. In practice, however, the standard of fair import expansion rather than non-discrimination has been applied to the three state-trading economies. In order to determine whether fair expansion of imports between the two areas was taking place, the respective trade flows were submitted to the control of the GATT forum.

It was only in the initial period of Poland's membership in the GATT (1968–70) that the GATT share in total Polish imports diminished. It dropped to 42 per cent in 1968 (as compared with 44–47 per cent in 1963–67) and fell even further in the next two years. From 1970 on, however, the GATT area began to account for an ever-increasing share of Polish imports – of machinery, raw materials, agriculture and consumer goods – and reached 64 per cent in 1974. This tendency is well illustrated in Table 6.5.

TABLE 6.5
Geographical Distribution of Polish Imports
(per cent)

	GATT countries	Czechoslovakia	Hungary	Romania	Non-CMEA GATT countries
1968	42.3	8.0	—	—	34.3
1969	41.8	7.6	—	—	34.2
1970	40.6	8.6	—	—	32.0
1971 ^a	43.9	8.8	—	2.0	33.1
1972	49.2	8.6	—	1.7	38.9
1973 ^b	61.6	7.7	3.4	2.3	48.2
1974	64.0	8.0	3.3	2.0	50.7

SOURCE: GATT documents and *Yearbook of International Trade Statistics*, 1974 and 1975 (Geneva: GATT).

^a Romania becomes a full member of the GATT.

^b Hungary becomes full member of the GATT.

The Hungarian and Romanian presence in the GATT coincided with an extremely dynamic development of these countries' imports from the GATT area. Romania's imports, for example, from the GATT countries increased by 61 per cent in 1974, exceeding by 14 per cent the rate of increase of total Romanian imports. Romanian imports from developed market economies increased in 1974 by 68 per cent in current dollars and the share of imports from these economies in total Romanian imports continued to rise from 45.5 per cent in 1973 to 51 per cent in 1974.¹⁹

After Hungary's accession to the General Agreement her imports from the GATT countries increased faster than total Hungarian imports. The spectacular import performance of Poland, Romania and Hungary from the GATT countries was not only due to an increase in volume but also to higher prices. It is worth noting that in 1974 import prices for the GATT area more than doubled for energy, increased by more than 50 per cent for raw materials and by nearly 25 per cent for foodstuffs.²⁰ Examination of the developments in Polish, Romanian and Hungarian imports which was conducted by the GATT was not related to evolution in relative prices within the GATT area and non-GATT area. Consequently, no conclusion as to the degree of discrimination between the two areas could be reached.

In general the GATT countries expressed satisfaction with the geographical development of Hungarian, Polish and Romanian imports. In that respect the three East European countries met the expectations of their GATT partners.

MULTILATERALISM

Did the accession of Hungary, Poland and Romania to the GATT bring a more multilateral character to these countries' trade with GATT members? Progress towards multilateralism in East-West trade was achieved primarily in two ways:

- (a) countries refrained from concluding new bilateral agreements after the expiration of the existing ones; or
- (b) rigid bilateral trade agreements were replaced by less rigid ones (that is, containing shorter product lists).

The progress towards multilateralism in payments is illustrated by Table 6.6.

A tendency towards multilateralism in East-West trade existed even before the three state-trading economies adhered to the GATT. It is thus difficult to determine to what extent progress in that respect is due to the membership of the East European countries of the GATT. It may even be argued that the aim of these countries—to get rid of discriminatory QRs—could clash with multilateralism. In the 1969 trade agreement between Poland and Denmark, for example, the removal of Danish

TABLE 6.6
Bilateral Payment Agreements

	Poland		Romania		Hungary	
	1968	1974	1971	1974	1973	1974
West Germany	D	D	D	D	D	D
United Kingdom	D	D	D	D	D	D
Italy	D	D	D	D	D	D
France	D	D	D	D	D	D
Austria	C	D	C	D	C	D
Sweden	D	D	D	D	D	D
Finland	C/D	D	C	D	C	D
Denmark	D	D	D	D	D	D
Benelux	D	D	D	D	D	D
Switzerland	C	D	C	D	C	D
Spain	C	D	C	D	C	D
Norway	D	D	D	D	D	D
Greece	C	C	C	C	C	C
Portugal	C	D	C	D	C	D

SOURCE: IMF Annual Reports on Exchange Restrictions 1961-73; United Nations Doc. ECE/Trade/176 Add.; and United Nations Doc. ECE/Trade/188, Add.

C = Rigid form of clearing (accounts have to be balanced).

C, D = Clearing permitting annual settling of accounts in convertible currency.

D = Settling of accounts in convertible currency.

discriminatory restrictions on Polish exports was paid off by the Polish undertaking to increase by 7 per cent annually its imports from Denmark.²¹

The GATT forum certainly provided pressure for progressive removal of bilateral arrangements which did not conform with its spirit. During their membership of the GATT, Poland, Romania and Hungary accepted clearing agreements with the 'GATT countries only where payment in convertible currencies would be difficult for the trading partners: this usually meant the less-developed countries. In general, the new bilateral payments agreements concluded by the three East European countries with the developed market economies, took into account the GATT commitment.

RECIPROCITY

Reciprocity in relations between Hungary, Poland and Romania, on the one hand, and their GATT partners, on the other, is examined under the assumption that the balance-of-trade criterion remains valid for judging the value of concessions (see Chapter 3).

To measure reciprocity between the East European members of the GATT and other GATT members according to balance-of-trade criteria, the following index may be used:

$$k = \frac{X - M}{X + M} 100 \%$$

where

X = exports of the country concerned to GATT countries

M = imports of the country concerned from GATT countries

For $k = 0$, that is for $X = M$, the balance of reciprocal costs and advantages is in equilibrium for the balance-of-trade criterion. The greater the value of k , the lower the degree of reciprocity reached.

The above index calculated for Poland, Romania and Hungary for the period of these countries' membership in the GATT shows the following results:

<i>Poland</i>	<i>per cent</i>
1968	-1.2
1969	-0.8
1970	6.1
1971	3.1
1972	-7.0
1973	-19.6
1974	-21.5

Romania *per cent*

1971 - 2.4

1972 - 4.4

1973 - 1.4

1974 - 4.6

Hungary *per cent*

1972 - 3.0

1973 - 0.3

1974 - 7.3

Except for 1970 and 1971 for Poland, the three East European countries were running a deficit on their trade account with the GATT countries. That deficit was particularly important for Poland in 1973 and 1974.

The three countries were seriously concerned with that state of affairs in the GATT forum.²² Though the situation was mostly due to new East European policies for obtaining credit in the West, it was also attributable to the fact that many West European countries discriminated against Poland, Hungary and Romania.²³ The East Europeans also feared their access to Western markets could be hurt as a result of the free-trade agreement concluded between the European Community countries and the EFTA countries, as well as the enlargement of the European Community.

All in all, the balance of mutual costs and benefits in terms of reciprocal market openings between Hungary, Poland and Romania on one hand and their GATT partners on the other was to the disadvantage of the three East European countries, at least according to balance-of-trade criteria. The situation could be attributed to other factors than those contemplated directly by the General Agreement – such as, for example, the East European credit policy. Once Poland and Hungary had decided to expand their imports from the West through the use of Western credits, however, they should have made this a bargaining point in the GATT. Their new market openings for Western products should have been exchanged for similar openings to East European products. In that sense, it could be said that both countries failed to use the concept of reciprocity to their advantage in the GATT.

CONSULTATIONS AND INFORMATION

The question of East-West trade ranked relatively low on the list of main concerns within the general GATT forum, due to three factors:

- (a) the relatively low quantitative importance of East-West

trade under the jurisdiction of the GATT;

(b) the technical character of East-West problems often marginal to general GATT debate on specific trade issues; and

(c) the fact that some aspects of East-West trade (for example, the problem of intra-CMEA trade and non-discrimination) were treated with 'kid gloves', keeping in mind political limitations.

The periodic consultations, provided for by the three protocols for accession, constituted the primary technique used to deal with East-West trade.²⁴

These consultations mainly had a rule – supervisory function, their rule-creating function being practically limited to two cases: modification of the Polish import commitment, and unsuccessful establishment of the final date for eliminations of discriminatory QRs on Polish exports. A substantial amount of consultation time was devoted to reviewing the past characteristics of East-West trade relations.

Periodic consultations provided a forum for successful settlement of several disputes in East-West trade.²⁵ The experience of East-West relations in the GATT, however, seems to suggest that when important trade interests are involved, the pressure of the GATT forum alone is often insufficient to force an adjustment. This was, for example, the case with the establishment of a terminal date for the transitional period for Poland.

A good example of the GATT's role in protecting East European interests involves enlargement of the European Community.²⁶ Poland's participation in negotiation of compensations for markets lost as a result of the enlargement of the Community was important. The negotiations permitted Poland to obtain significant compensations for the market losses occasioned by the accession of the United Kingdom, Denmark and Ireland to the Community.²⁷ Poland is the only country to have been considered twice in the Community's compensation offer. As a result of negotiations, about \$32.5m worth of Polish exports to the Community (based on 1973 trade) were influenced by the tariff compensation.

Finally, the informal GATT forum was important for resolving conflicts and furnishing inputs to the East-West commercial sphere. In fact, the informal consultations and negotiations provided a more frequent way of solving problems than the formal GATT procedure. The GATT Secretariat often acted as mediator, adviser and broker in helping to initiate dialogue between governments, carrying out information consultations on behalf of the East European governments with the Western governments, and providing competent advice on many technical issues.²⁸

The GATT joined its efforts to those of other international organizations to promote better exchange of commercial information between

East and West. The main source of GATT information on Polish, Romanian and Hungarian foreign trade was the background documentation supplied by governments for the periodic consultations. This included:

- (a) foreign trade statistics by four product groups: machinery and equipment, raw materials and semi-manufactures, food products, and consumer goods;
- (b) statistics on growth of GNP and trade (imports and exports) with two zones – GATT countries and all countries – divided into the four product groups listed above;
- (c) information on balance of payments; and,
- (d) other information on trade requested by any GATT member.

Participation in the GATT coincided with the improvement of Hungarian and Polish publications on foreign trade laws and statistics. After acceding to the GATT, Romania published the first volume of its annual statistics on foreign trade. It is probably no accident that, with the exception of the Soviet Union, the lowest level of statistical information on foreign trade is furnished by the non-GATT East European countries.

SUMMARY AND CONCLUSIONS

The GATT's contribution to East-West trade cooperation has varied considerably depending on the issues involved.

First of all, removal of conventional barriers to East-West trade in the GATT was certainly more modest than expected – both in the East and in the West. The GATT did not succeed in the immediate elimination of Western discrimination against East European exports: Poland, Romania and Hungary still suffer from the discriminatory quantitative restrictions directed against their exports by some West European countries. Moreover, Romania and Hungary did not obtain MFN treatment on the United States market upon entering the GATT. That state of affairs significantly limited East European benefits from participation in the General Agreement, though the GATT contribution to a progressive solution of these problems should be acknowledged.

On the other hand, neither the Polish nor the Romanian participation in the GATT liberalized their targets on imports from the GATT area. The Polish commitment to increase imports from GATT countries by 7 per cent a year became meaningless from 1970 on, since it did not entail any import increase in absolute terms. Neither Poland nor Romania, on the other hand, granted their GATT partners concessions on one-commodity or multi-commodity targets.

None the less, membership of the two countries in the GATT coincided with dynamic growth in imports from the GATT countries. Indeed, for the most part these imports increased faster than the GATT countries' imports from Poland and Romania. Therefore, according to balance-of-trade criteria, reciprocity has not been attained for Poland and Romania under the GATT. This state of affairs may be partly attributed to the fact that, in the GATT forum, neither Poland nor Romania was equipped with practicable and effective instruments of concession-making. The two governments had no real means of inducing their GATT partners to provide additional openings for products of interest to Polish and Romanian exporters.

The GATT's main contribution to East-West trade had been as rule-supervisor. The pressure of the contracting parties contributed to a progressive adjustment of the commercial policies and techniques relating Polish, Romanian and Hungarian trade to the GATT countries. The traders' forum supervised developments in the geographical and commodity distribution of Polish, Romanian, and Hungarian imports – bearing in mind the interests of the GATT countries and the conformity of these developments with the provisions of the respective protocols for accession. The East European countries in the GATT, thus, met the expectations of their partners in respect to dynamic development of imports from the GATT countries.

Pressure from the contracting parties also contributed to further multilateralization of East-West trade, although not sufficiently. It seems that this function of the GATT should be reinforced in the future.

Finally, the GATT forum of consultations provided a framework for protection of East European commercial interests. Poland, for example, successfully negotiated compensation for market losses resulting from enlargement of the European Community and took advantage of the GATT forum to discuss solutions of several other important trade problems.

NOTES AND REFERENCES

1. Rurarz, 'Comments', *Sprawy Międzynarodowe*, Warsaw, January 1975, p. 142.
2. It should be noted that imports from the West European countries for two December days equal about 1 per cent of total imports from the West. The Polish delegation cited this reason during the periodic review: see GATT *Basic Instruments*, 17th Supplement, 1970, p. 103.
3. *Ibid*, p. 103.
4. The average increase in world imports accounted at current prices amounted to 10.7 per cent in 1967–70 and to 20.7 per cent in 1971–73.
5. *Economic Bulletin for Europe* (New York: United Nations, 1975) p. 34.
6. *Polityka*, Warsaw, No. 9 (887), p. 13.

7. Balassa, 'The Economic Reform in Hungary', op. cit., p. 18.
8. Statistics indicated according to GATT doc. L/4228, October 1975, p. 2.
9. *Economic Bulletin for Europe*, op. cit., pp. 32-4.
10. See The United States Congress, *Trade Act* of 1974, sec. 402, Public Law 93-618 (Washington: US Government Printing Office, 1975).
11. This argument is not fully justified since the Polish import commitment is basically a counterpart of the contracting parties' tariff concessions.
12. GATT *Basic Instruments*, 17th Supplement, 1970, p. 109.
13. GATT *Basic Instruments*, 11th Supplement, 1964, p. 73.
14. *Basic Instruments*, 18th Supplement, 1971, p. 203.
15. *Ibid.*, p. 209.
16. Poland could have invoked Article XXIII of the GATT (nullification and impairment); however, the Polish government did not wish to go that far.
17. In 1967 about 50 per cent of Polish exports to the West were subject to discriminatory restrictions, in the United Kingdom about 50 per cent, in Italy about 20 per cent, in France and Austria about 20 per cent (on the basis of Polish statistics).
18. In the case of the United Kingdom, for example, most products liberalized in 1972 and 1973 fall under the Common Agricultural Policy of the Community.
19. *International Trade 1974/75* (Geneva: GATT, 1975) pp. 194-5.
20. *Ibid.*, p. 190.
21. This figure was fixed at 7 per cent in order to correspond to the figure for the Polish general commitment *vis-à-vis* the GATT countries. However, the arrangement visibly contradicted the meaning of multilateralism as practised in the GATT. Due to pressure from the GATT forum the character of the agreement was adopted to the GATT requirements See: GATT *Basic Instruments*, 17th Supplement, 1970, p. 100.
22. GATT Doc. L/4096, October 1974, p. 3; GATT Doc. L/3875, July 1973, p. 15-16.
23. GATT Doc. L/4096, p. 4; GATT Doc. L/3875, p. 16.
24. The consultations were conducted within a working party especially established for that purpose. Membership in the working party was not limited to any specific number, and in principle every GATT country interested could participate. This meant that during some consultations as many as thirty to forty delegations were present at a sitting.
25. The example of the Polish-Danish conflict, referring to discriminatory QRs may be cited. In January 1972 Denmark abolished some QRs on imports from the GATT countries but maintained them for East European countries including Poland. In the Polish view such action was contrary to Denmark's obligation *vis-à-vis* Poland under the GATT, since it increased the discriminatory element in restrictions applied by Denmark to imports from Poland. Poland brought the matter to the attention of the GATT countries during periodic consultations. The pressure of the GATT forum and the mediatory role of the GATT Secretariat brought the Danish authorities to agree on abolishing the discriminatory QRs on imports from Poland. See GATT *Basic Instruments*, 19th Supplement 1973, pp. 114-15.
26. The United Kingdom, Denmark and Ireland acceded to the European Community. Under the provisions of Article XXIV of the GATT, negotiations on compensatory adjustment may be required when a customs union is created.

Negotiations of this type took place under the GATT for the enlargement of the Community within the working party especially established for that purpose between March 1973 and July 1974. Nineteen GATT governments participated in these negotiations.

27. The Polish list of claims included the following elements: (i) Poland suffered a loss in exports of some products to the British, Danish and Irish market as a result of application by the three countries of a Common Agricultural Policy; (ii) Poland suffered a loss in exports of some products to the British, Danish and Irish market due to increase of some duties; the enlargement of the Community brought about an increase of the average tariff rate for Polish exports to the Community (especially for products like steel, flax, and some agricultural products); and, (iii) Poland ceased to be a principal supplier of some products to the three markets. For example Poland used to be a principal supplier of fur-topped boots on the British market, but is a marginal supplier of that product on the Community market and consequently lost the possibility of influencing the level of the tariff on that product in Britain. The problem is extensively discussed by Tomasz Bartoszewicz, 'Rozszerzenie EWG a GATT', *Sprawy Międzynarodowe*, Warsaw, March 1975, pp. 128–34.

28. The following is an example of the Secretariat's role in solving problems of East-West trade. In November 1971 Italy imposed discriminatory restrictions on exports of fertilizers from Eastern Europe. In the Polish view, this was contrary to the obligations undertaken by Italy under the GATT and likely to entail some loss of export possibilities for Polish producers of nitrogenous fertilizers (the main product of interest to Poland). Poland estimated that the loss would amount in the following year to \$1m. Informal consultations took place between Poland and Italy; however, no agreement could be reached. Before the official consultations under Article XXII:1 of the GATT took place, the Director-General of the GATT – Olivier Long – acting on informal demand by Poland, got in touch with the Italian government. He stressed the view of the Secretariat on the question and seemed to suggest the Polish complaint was '*bien fondé*'. As a result of this intervention, Italy decided to remove the discriminatory restrictions against Poland.

Proposals for East-West Trade under the GATT System

Let us first briefly draw together the strands of analysis of this book and relate them to some particularly disturbing features of East-West trade cooperation. Next, let us consider some suggestions for change in the present East-West trade arrangements in the GATT.

CONCLUSIONS

MECHANICS

A principal theme of this book has been that Poland, Romania (and Czechoslovakia) as members of the GATT did not dispose of an effective instrument for concession-making. The respective reciprocity arrangements were fictitious and were the result of the unwise East European strategy to participate in the GATT at very little cost in terms of commercial commitments. Since nothing may be obtained 'for free' in a traders' forum such as the GATT, not much was granted to the East European countries in terms of better access to the Western markets. Paradoxically, however, important market openings have been granted by the East European members to their Western partners. Indeed, imports of the East European GATT members from the GATT countries have increased spectacularly during recent years – mostly as a result of a new credit policy in the East-West sphere. Since they did not dispose of concession-making instruments in the GATT forum, East Europeans were not able to use their import increases (market openings) as a bargaining element to obtain reciprocal market openings in the West. This brings us to a conclusion (which is absurd *prima facie*) – that as long as GATT countries continue to 'play' on reciprocity, it is paramount for the interests of the East Europeans that they render their reciprocity arrangements effective; the more so that other arguments

may be advanced to justify a search for a balance of costs and benefits in the East-West sphere.

(a) Socialist countries' exports to the West have not grown sufficiently to finance those countries' import spending. This was partly due to relatively bad access of the East European products to the Western markets and particularly those of Western Europe (protected by the discriminatory QRs). Consequently, the spectacular import increases of Poland and some other East European countries in the GATT could only be made possible by foreign credits to finance the growing balance-of-trade deficit. The indebtedness of Poland, Romania and Hungary, however, is likely to reach acceptable limits very soon. Therefore, the future development of Western exports to the East European markets is directly dependent on the growth of East European exports to the West. It seems necessary to translate this obvious truth into concrete action at the Tokyo Round. The balance of cost and benefits, especially between Western Europe and the Socialist country members of the GATT, must be re-established, if trade between the two groups is to develop along some dynamic path.

(b) The balance-of-payments criterion of reciprocity, as has been shown, is likely to gain in relative importance in the East-West sphere (Chapter 3).

(c) Finally, an effective East-West reciprocity arrangement in the GATT might be of particular interest to small- and medium-sized traders. The spectacular development of East-West trade has been till now, to a large extent, assured by large Western corporations, powerful enough to find their way to Eastern Europe even without GATT assistance. Effective reciprocity arrangements could be of great help to less powerful but competitive enterprises willing to trade with Eastern Europe. That in turn could contribute considerably to further dynamic growth of East-West trade flows and modification of their structure in favour of consumer goods imports by the CMEA countries.

The most important shortcoming of GATT provisions on non-discrimination in East-West trade is due to the fact that they do not relate explicitly enough to the planning techniques in Eastern Europe. Though some standards of non-discrimination under central planning might be laboriously deduced from the GATT provisions on direct trade control, there are still important omissions when those discrimination standards are to be applied to target-protected systems (Chapter 3 and Chapter 5).

The GATT's pragmatism was particularly apparent in the economically and politically important issue of CMEA integration. GATT

countries did not really insist that intra-CMEA trade conform with the provisions of the GATT. Given the political environment, East European integration could not be a subject for negotiation in the GATT. The contracting parties chose to ignore the existence of the CMEA at least as a legal problem in the GATT even though the issue concerned one of the most disturbing features of East European commercial policy.

Some *de facto* accommodation has occurred, however, through what could be termed the 'fair expansion' of imports within the non-CMEA and the CMEA area.

In the case of Poland this was achieved indirectly by requiring that the quantitative growth of Polish imports from the GATT countries and from the non-GATT countries (mostly the centrally-planned economies) be carefully supervised during periodic consultations. Romania promised to plan its imports so as not to diminish the share of imports from the GATT countries in her total imports. Only the Hungarian protocol explicitly refers to trade relations with the centrally-planned economies and imposes limits on the increase of preferences in trade relations with these economies.

Nevertheless, the concept of 'fair shares' in import expansion from GATT and non-GATT countries is more political than economic in nature. It says nothing about protection though in economic terms protection is what integration is about.

Some rethinking of the GATT approach towards the integration problems of the state trading systems may be required since the GATT environment has changed considerably.

Western political arguments against the recognition of the CMEA as a regional grouping in the GATT have lost much of their relevance (Chapter 1). The new policy of the European Community towards the CMEA certainly marks a departure from the policy of differentiation among the East European countries. Since the Community is presently the main initiator of the '*Ostpolitik*' in the GATT it may have a direct impact on the attitude of the GATT towards East European integration.

The possible intensification of economic integration within the CMEA is likely to increase pressure from West European countries to include these developments within the GATT sphere of competence. Moreover, the CMEA integration coincides with a tendency of the East European countries towards the creation of dual foreign trade systems. Whereas trade among the CMEA countries continues to rely on plan targets and virtually fixed prices, tariffs are being progressively introduced in trade with the Western market economies. This poses a technical problem when comparing commercial treatment within the two areas.

Finally, there is the new issue of preferential trade agreements between the tariff-protected and target-protected economies. Some East

European countries, troubled by undesirable repercussions on their export interests arising from the enlargement of the European Community, have concluded free trade arrangements with Finland and are considering the possibility of similar arrangements with some other market economies.¹ An examination of the Finnish-Hungarian arrangement in the GATT has revealed enormous difficulties in dealing with the integration problems of the centrally-planned economies on the basis of GATT provisions. At the time of writing, no agreement has been reached on the conformity of the arrangement with Article XXIV, and great difficulties may be expected.

All these developments speak in favour of some modification of the GATT's approach to the integration problems of Eastern Europe.

There might be also a need to modify the present reporting procedure on functioning and new developments in East-West trade policy. Indeed, the GATT scrutiny of protectionist and discriminatory policies in that sphere, though of great merit, consists to a large extent of formalistic statements to be found in the countries' notifications or replies to the questionnaire on state trading. It seems that more emphasis should be put on countries' notifications regarding issues which are likely to raise suspicions of non-conformity with the rules of the GATT.

Moreover, insufficient use is made of GATT consultation procedure in the East-West sphere. Indeed, a substantial amount of consultation time was devoted to examining the past characteristics of trade development or governments' actions, whereas rule creation and discussion of trade policy issues likely to arise in the future was limited. Neither were the *ad hoc* consultations sufficiently used. Some West European countries, for example, long complained about market disruption by their East European partners, but no use has been made of the relevant provisions of the GATT for consultations on this matter.²

Finally, the observer of East-West trade relations will easily identify important issues of East-West trade cooperation which have escaped the competence of the GATT. Indeed, East-West trade relied considerably on industrial cooperation and barter trade techniques such as switch-trading and private compensation and specific forms of government assistance in export promotion. It might thus be desirable to consider a much larger approach to include those aspects into the sphere of concern of the GATT as well.

POLITICS

When judged from the political perspective, the GATT East-West arrangements are second-best solutions – both for the socialist bloc and the West. The GATT did not really succeed in becoming an instrument of Western policy and differentiating among individual members of the

CMEA. Indeed, despite the favouritism displayed toward the East European countries admitted to the GATT, Washington and Western Europe did not really grant them better commercial treatment than those East European states remaining outside the organization. This was reflected particularly in Washington's refusal to accord MFN treatment to Hungary and Romania during the initial period of their membership of the General Agreement. It is still apparent in the policy of some West European countries in respect to discriminatory QRs on East European exports.

In the view of the Socialist bloc, the country-by-country approach towards East-West trade cooperation has resulted in a differentiation of the GATT solutions for trade with Eastern Europe. Moreover, the country-by-country approach, *ad hoc* in nature, is also one of the most important reasons for Moscow's dissatisfaction with the present GATT pattern of East-West cooperation. It is interpreted as an effort to put the East European countries in a position of second-category members (Chapter 1). Consequently, it could be claimed that incorporation of provisions relating to the target-protected and state-trading systems, as alternative forms of organizing foreign trade systems, could be desired for the GATT. Reforms along those lines could render the GATT more acceptable to the Soviet Union and some other socialist countries and thus could contribute to the trend towards the universalism of the General Agreement. For the West this modification would not cost very much in political terms. After all, the GATT has long ceased to be an instrument of the Western policy of differentiation among the various governments of Eastern Europe.

A second important issue for the socialist bloc is the establishment of an effective link between the GATT and the political organs of the United Nations. On this point the East European task is practically identical with that of some developing countries whose aim is the restructuring in their favour of present unjust trade relationships. This tendency is reflected, for example, in the recent report of a group of experts to the United Nations General Assembly. The report recommends that:

GATT and the United Nations enter into a mutually satisfactory agreement providing for a formal relationship, including exchange of information and closer administrative collaboration.³

Finally, the Socialist bloc supports the idea of stronger links and better policy coordination between the GATT and UNCTAD which currently act as rival bodies. It has already been suggested that an international trade organization incorporating UNCTAD and the GATT be established, and a 'commodity chamber' be eventually created.⁴

There is also evidence that the creation of a comprehensive trade organization, either on the basis of the GATT or independent of it, still remains the ultimate goal of the socialist bloc in matters of the international economic order (Chapter 1). Followers of the fundamental reforms recognized that 'any structural change in the field of trade should not be allowed to interfere with the multilateral trade negotiations now being carried out under GATT auspices'.⁵ Indeed, the negotiations are expected to produce by the late 1970s the most comprehensive and complex agreement ever reached on the reduction of tariffs and non-tariff barriers as well as on some elements of the international trade system. Once the trade experts return home, however, the political conflict of interests around the GATT and a proposed comprehensive trade organization is likely to arise again.

Drawing together the strands of the above analysis, it may be claimed that some rethinking of the present East-West GATT arrangements may be required if the GATT is not to restrict its role in the ever more important sphere of East-West trade. Proposals for reform may be worked out on the basis of two alternative assumptions.

(a) The GATT should aim at an improvement of the existing technical arrangements maintaining, however, its present stand on the country-by-country approach, the integration issue *et cetera*.

(b) New approaches should be considered to adapt the GATT to changed economic and political realities of East-West cooperation.

PROPOSALS AND PROSPECTS

IMPROVING THE EXISTING ARRANGEMENTS

This may be considered from two angles. The first is to improve the negotiation of concessions on the basis of targets. The second is to consider the likelihood of a wider participation of the East European countries in the GATT on the basis of tariffs.

It has been shown that negotiations on specific import targets of the East European countries maintaining target protection could have been conducted under existing provisions (Chapter 5). Thus it is a change in the negotiation strategy, rather than in the drafting of the respective protocols for accession, that is needed to render the East-West reciprocity arrangements more effective.

It has sometimes been argued that granting of concessions on specific import targets would further limit the East European countries' bargaining position on international markets (Chapter 5). The argument is rather weak or at least not universally valid. Are not the important intended purchases by the centrally-planned economies

known in Western business circles long before transactions are concluded? They are known in a majority of cases. The announcement of the specific import targets in advance could not only provide a suitable bargaining element but could constitute a sort of request offer in the West as well. In that manner a greater number of Western industries and exporters competing for East European markets could be attracted and purchases conducted on better terms than otherwise. The following solution might be suggested to make the scheme work.

Each of the countries mentioned should choose five to eight importable products of particular interest to its main GATT partners and negotiate concessions on its respective one-commodity import targets. This would mobilize those Western industries especially interested in these particular openings to support the demands of Poland, Romania and Czechoslovakia for reciprocal import openings by Western governments. The granting of concessions on one-commodity import targets could thus bring about a considerable improvement in the bargaining position of the target-protected economies in the GATT. It could, for example, accelerate the removal of the remaining discriminatory QRs on Polish, Romanian and Czechoslovak exports and constitute an important bargaining instrument in multilateral trade negotiations.

An important weakness of the present GATT arrangements for Poland is the method of calculating the import commitment. It has been shown that inflation and the reduction in value of the dollar in terms of other Western currencies have made this commitment meaningless.

The commitment could be rendered meaningful by calculating import performance at constant dollar prices rather than current dollar prices (as is now the case), or by some other method thereby eliminating the impact on Polish imports of inflation and fluctuation in exchange rates. Modification along these lines, however, would considerably increase the burden of Polish obligations under the GATT without bringing any reciprocal advantage.⁵ It is thus doubtful that the Poles would be interested in any move of this kind. On the other hand, however, Poland might be interested in renegotiating its arrangement with the GATT so as to render the balance-of-trade criterion of reciprocity more evident in the reciprocity formula. It may be that a proposal aimed at reconciling Polish and Western interests might prove realistic.

An alternative method of solving the reciprocity problem in the East-West trade would be to adopt the traditional tariff approach of the GATT, as for example was done for Hungary. A solution along those lines, however, should depend on the degree of decentralization in the East European foreign trade systems. The idea is slowly gaining some new ground in the GATT and may require some investigation.

There is a clear tendency in Eastern Europe (with exception of the Soviet Union and the German Democratic Republic) towards replacing

target by tariff protection. Indeed, the economic reforms in many East European countries over the last decade involved decentralization of both planning and foreign trade monopoly institutions. A closer automatic link between domestic and foreign prices has been introduced and both Poland and Romania have initiated customs tariffs as supplementary instruments of trade control.⁶ Those reforms coincided with a rising conviction in Poland and Hungary that the respective countries' membership in the GATT should be based on a tariff rather than an import commitment basis.

The GATT working party set up to examine the Romanian tariff system as a possible instrument for Romanian participation in the General Agreement ran into major difficulties. Romania's contention, that its tariff system constitutes the main protective element not only against the market economies but also against the centrally-planned economies, is in fact based on very scant evidence. The system is certainly more centralized than Hungary's was in 1973. There may well be some doubt as to the effectiveness of the Romanian tariff system as an instrument of trade control and the granting of concessions. Romania's trade with the centrally-planned economies continues to be based on plan targets and virtually fixed prices. Consequently, tariffs can only assume a very limited role as a supplementary instrument of trade control.⁷

Romania's efforts to participate in the GATT on the basis of its tariff system are likely to be opposed by the European Community and other West European nations particularly concerned with the issue. The outcome of this case will no doubt considerably influence the future Polish, and possibly also the Bulgarian, policy on tariffs.⁸ The issue is thus of great importance and it may be useful to state briefly the pros and cons of a more extensive tariff-based membership of state-trading economies in the GATT.

For:

(a) The present Polish commitment and Romania's undertaking under the GATT's schedule of concessions are practically meaningless. The GATT countries have thus nothing to lose but something to gain in accepting the Polish and Romanian tariff approach.

(b) The acceptance of the tariff approach to other East European countries in the GATT would conform to the political aspirations of the West to induce the centrally-planned economies towards decentralization.

(c) The GATT is essentially a tariff agreement. The participation of the state-trading countries in the Agreement on a tariff basis would be a step towards uniformity of relations among the member nations of the GATT.

Against:

(a) It would probably be a long time before the Polish, Romanian or Bulgarian tariff systems became fully effective even in trade with the West.⁹ Thus, tariff-based participation of these countries in the GATT would be only theoretical, at least in the initial transitional period.

(b) Tariff-based participation in the GATT would in turn limit the practical significance of GATT membership both for the country in question and for its trade partners (see the case of Czechoslovakia). Moreover, it would also work against the 'clarity' in application of the rules of the GATT.

To reconcile these contradictory views, one could propose that the eventual participation of Poland or Romania in the GATT on a tariff basis should be preceded by a transitional period. At the end of this period, if tariffs proved effective, the quantitative undertakings could be replaced by tariff concessions.

A move by some East European countries from a target-protected system towards a tariff-protected one might enable them to participate in the GATT virtually along the lines of the traditional GATT pattern. The Hungarian example is likely to be considered a minimum standard of decentralization for a valid tariff approach in the GATT.¹⁰

Some improvement in the GATT scrutiny of protectionist and discriminatory policies in the East-West sphere could be achieved by supplementing the present notification requirements by some additional points. This could be done either by adopting the present GATT questionnaire on state trading to the needs of the East European GATT members, or introducing new elements in the notification procedure under the respective protocols for accession. The modification should refer particularly to the following points.

(a) Independence of the state-trading units from state authorities:

- absence of day-by day interference in the operation of state-trading units by state authorities (other than periodically issued plan targets);

- evaluation of the commercial activities of state-trading units by organizations other than those which supervise execution of the foreign trade plan;

- for tariff-protected economies, assurance that no import targets are maintained on imports from the market economies.

(b) Non-discrimination:

- declaration that no import targets specific to any particular country are maintained for trade with GATT countries;

—confirmation that the state-trading enterprises are not induced to discriminate by other methods contrary to the GATT principles.

(c) Competitive situation and price formation:

—methods adopted by the government to assure that monopolistic traders and producers do not enjoy protection in excess of that provided for in the country's tariff schedule (for the tariff-protected economies);

—other information on the competitive situation of the market; assurance that no measures have been introduced to limit free price formation and provide protection exceeding that indicated in the tariff schedule (for the tariff-protected economies).

Extended reporting along the above lines would help to identify any discriminatory and protective devices in the state-trading countries. It might also prove advantageous to these countries. The East Europeans have often suffered in the GATT from prejudice against their economic systems — prejudice often resulting from ignorance about central planning and the functioning of state trading. In the business world matters about which little is known are often interpreted to their disadvantage.

In respect to periodic consultations, efforts should be made to initiate the discussion on those problems of East-West trade which are likely to arise in the near future. The consultations forum could in that way acquire a function of guiding new developments and rule-creating rather than limiting itself mostly to rule supervision.

Finally, it has been suggested that the creation of a separate GATT body for East-West trade might improve the GATT's management capacity in the East-West sphere.¹¹ The usefulness of such a solution, however, is questionable; and the GATT should probably attempt to integrate specific East-West issues into its general working structure rather than isolate them. One wonders, moreover, whether the GATT needs a new forum for discussion. Negotiations under the General Agreement are usually conducted in the GATT working parties, convened on an *ad hoc* basis; and government officials have sufficient opportunity to exchange views in informal meetings in Geneva. There is also the problem of a conflict of competence among the various international organizations in which discussion on East-West issues takes place, for example the Economic Commission for Europe, UNCTAD, the United Nations, ECOSOC, and others.

Nevertheless, the GATT's contribution to the East-West sphere could be improved considerably through the following initiatives.

The GATT Secretariat could assign a group of experts to prepare reports on commercial relations with the state-trading economies from the perspective of the GATT. GATT services could also be used more extensively in the management of East-West trade relations. For example, more extensive work in this respect (preparing studies,

arranging consultations between exporters, and so on) could be undertaken by an UNCTAD/GATT International Trade Centre.

CONSIDERING NEW APPROACHES

Discussion on a new GATT approach towards East-West trade cooperation should probably be conducted with the possibility of eventual more extensive participation of the socialist countries in the GATT borne in mind. The absence of the Soviet Union, China and some of the other centrally-planned economies in the General Agreement considerably limits the GATT's role in the ever more important sphere of East-West trade, and introduces a risk of the gradual political self-destruction of the GATT as a world forum of traders.

The first objective should probably be to introduce into the General Agreement provisions explicitly referring to the target-protected and state-trading systems, recognising those systems as alternative methods of organizing a country's foreign trade. Indeed, in this respect the present GATT arrangements for East-West trade are even less satisfactory than those offered by the American 'Suggested Charter' and to some extent the Havana Charter of thirty years ago (Chapter 1). The General Agreement should incorporate new provisions on non-discrimination under plan targets. It should also provide for a reciprocity arrangement, along the lines of the American 'Suggested Charter' and contain a clearly set code of conduct on dumping, market disruption and safeguard clauses, adapted to the conditions of the centrally-planned foreign trade systems. Respective provisions should refer to planning techniques rather than rely on general statements and assurances.

A particularly difficult task would be to translate the GATT concept of regional integration (Article XXIV), based on the tariff approach for needs of the target-protected economies. One possible criterion for the acceptable integration of the centrally-planned economies might have been the extent to which the integrated area is controlled by one planner (Chapter 3). More precisely, a uniform foreign trade plan could be necessary, with a common import target determining a common explicit rate of tax with respect to third countries.

Another approach could be based on the assertion that the import mark-up rates on trade between two (or more) state-trading systems should be progressively reduced, through target liberalization and domestic price adjustments.

Modifications along those lines could be introduced either by incorporating some new provisions into Article XXIV or by according a waiver under that article.

Proposals on East-West trade cooperation can hardly be firm and dogmatic since the issues they deal with are highly controversial both in

economic and political terms. If this book has contributed a small and modest amount towards the better understanding of the the problems of multilateral trade arrangements between the centrally-planned and the market economies, then its objective has been reached. To underline the purpose of this type of study it seems appropriate to conclude with Wilhelm Roepke's words:

... whereas the text-books ... show that international trade rests on the law of comparative costs, its foundation is, in the last resort, the categorical imperative *pacta sunt servanda*.¹²

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1. Finland has concluded free-trade arrangements with the following East European countries: Bulgaria, Czechoslovakia, Hungary, the German Democratic Republic and Poland. The GATT working party examined this issue in September and October 1975. (See GATT Doc. L/4230, October 1975, p. 7.) The German Democratic Republic and Bulgaria, which are not members of the GATT, refused to be a party to any examination by the GATT of their free-trade arrangement with Finland.
2. It is only recently that the European Community has asked for consultations with Poland, Romania and Hungary on market disruption under the respective provisions of the protocols for accession (para. 4 of the Polish and Romanian protocol and para. 5 of the Hungarian protocol).
3. See *A New United Nations Structure for Global Economic Co-operation*, E/AC. G2/9 (New York: United Nations, May 1975) p. 55.
4. *Ibid.*, p. 54.
5. *Ibid.*, p. 55.
6. These tariffs were characteristic of a developing country. Rates were very high on a majority of consumer goods and relatively low on machinery, raw materials, *et cetera*. For example, in Poland in 1976 consumer goods were subjected to average rates of about 40 per cent, raw materials to rates of 0–5 per cent, semi-processed goods to rates of 6–15 per cent and finished products to rates of 25 per cent (GATT Doc. G/M/112, February 1976, p. 13).
7. The function of tariffs under a multi-commodity target is discussed in Chapter 3.
8. Bulgaria intends to participate in the Tokyo Round negotiations on the tariff basis. An experimental tariff system has already been set up in Bulgaria *vis-à-vis* the market economies.
9. The introduction of an effective tariff system in Yugoslavia took several years of foreign trade and economic reforms, in spite of a favourable political environment for decentralization. In the case of Poland an effective tariff system would certainly require first of all price reform. This in turn might be unacceptable on political grounds. See, for example, the violent reaction of the Polish workers to price increases for some consumer goods in December 1970, which resulted in the departure of Gomulka's group, or the unsuccessful attempt to increase prices of some consumer goods in July 1973.

10. Some GATT members have complained about the progressive centralization of the Hungarian economic system since its accession to the Agreement. (GATT Doc. L/4230, October 1975, p. 4, and GATT Doc. L/4228, October 1975, p. 6.)

11. This might be for example a group of experts on East-West trade functioning on a permanent basis.

12. Wilhelm Roepke, 'Economic Order and International Law', *Recueil des Cours* (de La Haye), vol. II, 1954; p. 212.

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